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THE UNIVERSITY OF ALBERTA

CANADIAN MERGER LAW 1986

BY

Ⓒ ROBERT G. GATEMAN

A THESIS
SUBMITTED TO THE FACULTY OF GRADUATE STUDIES AND RESEARCH
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OF MASTER OF LAWS

FACULTY OF LAW

EDMONTON, ALBERTA
FALL, 1986

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RG Gateman

ROBERT G. GATEMAN
Edmonton, Alberta
Canada

Date: 9 October 1986

THE UNIVERSITY OF ALBERTA

FACULTY OF GRADUATE STUDIES AND RESEARCH

The undersigned certify that they have read, and recommend to the Faculty of Graduate Studies and Research for acceptance, a thesis entitled CANADIAN MERGER LAW 1986 submitted by ROBERT G. GATEMAN in partial fulfilment of the requirements for the degree of MASTER OF LAWS.

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To

Jane and Meaghan

ABSTRACT

In June of 1986, the Combines Investigation Act, which had come to be viewed as completely ineffectual as a policy tool to scrutinize and prevent anticompetitive merger activity in Canada, was radically amended. A new quasi-judicial Competition Tribunal, composed of both judges and laypeople, will now adjudicate an application by the Director to modify or prohibit a merger or proposed merger. The review of the suspect merger under the companion Competition Act will focus on whether competition is or is likely to be lessened substantially. As a reviewable trade practice, the new merger provisions will be subject to the civil burden of proof. A major innovation in the Competition Act is to require relatively large proposed mergers to notify the Director of their intention, to supply information which might be helpful in evaluating the effect of the merger on competition and to wait for a prescribed period of time before proceeding with the transaction. This paper reviews the numerous proposals for merger reform preceding the new Act with the intention of discovering the policy rationale or economic justifications for the specific provisions adopted in the Competition Act. An examination of the redefined jurisdiction of the Competition Tribunal and the investigatory powers of the Director reveals that the constitutional challenges under the former Act have probably been avoided. The proposition is adduced that the only practical means of preventing potentially harmful mergers is to employ the injunctive relief provisions; the usefulness of these remedies, however, is contingent upon an enlightened interpretation of the substantive provisions. Finally, this paper explores the feasibility of developing administrative guidelines to assist the Director, and the business community, in determining when an application for provisional injunctive relief should be brought. The paper concludes by emphasizing the strong possibility that expectations of a tougher merger policy may be overly optimistic.

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The art of thinking is a noble aspiration but one to which few people find themselves in close proximity. Throughout the somewhat prolonged process of completing this paper, I have discovered that my patient advisor, Professor Robert Nozick, is a member of the select group which has acquird this art. In the future, I suspect that my recollection of the intricate workings of the Competition Act may be somewhat obscure, however my desire to develop the skills which he has acquired shall remain. I wish to thank Professor Nozick for the hours and hours of his time, the consideration, encouragement and most of all ideas that he has offered freely to me. Thanks.

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Finally, any errors in this paper should case no dispersions whatsoever on those people who have assisted in the preparation; as always, any errors are completely the responsibility of the author.

Robert G. Gateman
Edmonton, 1986.

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I INTRODUCTION

A PRINCIPAL OBJECTIVE

> On June 19, with little fanfare, legislation took force that radically alters the legal stage on which takeovers and mergers are permitted in Canada.[1]

Great expectations accompany the enactment of the new Competition Act.[2] The merger provisions of the former Combines Investigation Act were viewed as completely ineffectual, with not one successful prosecution of a contested case in the 75 year history of combines legislation. Acknowledging that the former merger provisions were less than effective, the almost universally accepted presumption is that the current reforms will impose more restrictions on mergers and proposed transactions. Evidencing this view, Jennifer Lewington surmised:

> The Reagan Administration is working to relax U.S. antitrust laws, while Canada recently toughened [emphasis added] its rules on corporate mergers. But, from different directions, the two countries are actually aligning their appraoch to combines law, antitrust experts say.
>
> "There is a general and gratifying impression that there's convergence of U.S. and Canadian antitrust policy," said a U.S. Justice Department official of recent trends in both countries. "With the degree of integration between the U.S. and Canadian economies, it leads to smoother relations when our respective policies are approached similarly."
>
> Historically, the United States has been at the forefront of tough antitrust enforcement, with federal laws dating back to 1914 and 1890.
>
> . . .

---

[1] Edward Greenspon, "Federal Tribunal Sets New Stage For Mergers", August 18, 1986, Globe and Mail B1.

[2] Competition Act, S.C. 1986, proclaimed June 19, 1986, excepting s. 80-99.

> In Canada, the move to a modestly tougher [emphasis added] merger law has come only after more than a decade of debate and compromise between the government and the business community.[3]

However, evidence is mounting that these more restrictive provisions may be inadequate to the task. The purpose of the following study is to ascertain how far short the actual reforms fall from their anticipated objectives.

Essentially as a result of three merger judgments and subsequent incisive commentary, it was perceived by most that the proscriptions against mergers under the former Combines Investigation Act had been enervated. It was generally conceded that the criminal forum necessitating proof beyond a reasonable doubt was not the appropriate setting to deal with the extremely complex array of economic and political factors governing the evaluation of merger activity. Constitutional questions had been raised about the propriety of the Act itself, as well as of the investigatory powers established pursuant to Part I of the Act. Furthermore, serious controversy surrounded the test of illegality. The two-pronged condition necessitating proof that the merger lessened, or was likely to lessen, competition to the detriment or against the interests of the public was seen as presenting an insurmountable hurdle to the prosecution of even the most flagrantly unacceptable merger. Of all the shortcomings, the inability of the former provisions to deal with mergers prior to consummation weighed heavily on the minds of the policy analysts. Thus, an indepth review of the concerns, both real and apprehended, surrounding the former merger provisions is then necessarily an integral component of this paper.

---

[3] Jennifer Lewington, "Canadian, U.S. merger laws converging", July 29, 1986, Globe and Mail B6.

In response to these concerns, a long succession of proposals for reform and draft bills extending over three decades were introduced. Four "proposal waves" filled the years preceding the current amendments. The first, the Economic Council of Canada's Interim Report of 1969 formed the basis for the Stage I amendments to the Combines Investigation Act, finally enacted in 1976. Second was the 1976 Skeoch-McDonald Report, which was far-reaching in its implications and which supplied the theoretical foundation for Bills C-42 and C-13. The third wave of recommendations commenced with the 1978 publication of the Report of the Royal Commission on Corporate Concentration and culminated in Bill C-29 in 1984. This Bill was in many ways the forerunner of the new Act. The final surge was initiated by the new Conservative government's 1985 Consultation Paper, which led to Bill C-91 and eventually to the new Competition Act. This history of reform is outlined in more detail in chapter I in order to highlight the public policy issues under scrutiny and in order to underscore the inherent difficulties in constructing an effective, policy-driven yet flexible and equitable merger policy for Canada.

The Competition Act establishes the rules within which the game of corporate takeovers is to be played; the Competition Tribunal Act elects the referee. To date, the merger provisions are untested. Obviously, the interpretation given the provisions by the courts, the Tribunal and the Director will all affect the practical application and effectiveness of the reviewable merger provisions. Therefore, the primary purpose of this paper is to investigate the reform in order to evaluate the progress since the Combines Investigation Act and to anticipate any operational pitfalls.

B TEXT ORGANIZATION

This paper is divided into ten chapters including the introduction of chapter I and the concluding remarks found in chapter X. A detailed outline of the history of reform is supplied in chapter II. Chapter III reviews the companion Competition Tribunal Act and emphasizes the hybrid nature of the new Tribunal. Whereas the shift to civil procedure was uncontentious, the issue over the proper forum in which to review merger activity was not. Although not within the major purview of this study, an analysis of the recent changes would be incomplete without recognizing that possible constitutional challenges which may plague the investigatory powers of the Director under Part I of the Act. Consequently, chapter IV explores these issues.

The effectiveness of or need for all the provisions of the new merger legislation rests squarely on the substantive test enunciated in sections 63 to 70 of the new Act. The degree of effectiveness accorded these provisions will in turn determine two subsequent issues: (1) the necessity to require pre-notification and (2) the efficacy of provisional injunctive relief. The new standard, which establishes the relative desirability of a mergers, is discussed in chapter V. Regardless of the possible results under the substantive provisions, certain "transactions" will be required to pre-notify the Director and the parties will be obliged to supply the Director with specific information characterizing the merger and its potential anticompetitive consequences. These complex pre-merger requirements are detailed and evaluated in chapter VI. If the Director suspects that the merger would be subject to a remedial order, injunctive relief temporarily halting the transaction may avoid the otherwise almost impossible task of disentangling the enterprises. Chapter VII, then, studies the new provisions for preliminary and interlocutory injunctions.

Chapter VIII and IX examine the present American Merger Guidelines with a view to adopting similar administrative guidelines to govern the application for provisional injunctive relief under the Competition Act.

It has been intended in this paper to focus on the pre-notification and injunctive relief procedures in the Competition Act. As well, emphasis has been directed towards the delineation of the relevant market and its relation to the substantive test criteria.

The objective of the paper is not to provide conclusive commentary since this will obviously require several years of challenging the provisions before the Tribunal and the courts but, instead, to formulate and provide informed expectations of the likely performance and potency of the recently enacted merger provisions.

II THE HISTORY OF CANADIAN COMPETITION POLICY LEGISLATION

A INTRODUCTION

The legislative history Canadian Competition Policy is most easily summarized by reviewing the relevant reports and studies in the area in conjunction with the changes and proposals for change in the legislation over the past ninety-seven years. Only three superior court cases under the substantive tests were considered in the past twenty-five years.

The history of competition legislation[1] is divided into four chronological sections. The first is a cursory overview of developments prior to 1950. The second deals with major developments following the MacQuarrie Report.[2] of 1950. The two unsuccessful merger prosecutions in 1960 set the stage for the following decade of merger investigation. Finally, since 1969, four reports have supplied the impetus for varied reforms to Canadian competition policy. The Economic Council's Interim Report, 1969, shaped both Bill C-256 and Bill C-227; the Skeoch-McDonald Report molded Bills C-42 and C-13. In 1978, the Royal Commission Report assuredly influenced the 1981 Proposals and Bill C-29. And finally, the Conservative government's 1985 Consultation Paper was the forerunner of Bill C-91 and eventually the present Competition Act.

---

[1] For a detailed history of the legislation prior to 1950 see:
J.A. Ball, Canadian Anti-trust Legislation, Baltimore: Williams & Wilkins, 1934.
R.F. Gosse, The Law on Competition in Canada, Toronto: Carswell, 1962.
MacQuarrie Report, Ottawa: Queen's Printer, 1952.
J.M. Magwood, Competition Law of Canada, Toronto: Carswell, 1981.
G. Rosenbluth and G. Thorburn, Canadian Anti-Combines Administration, 1952-60, Toronto: University of Toronto Press, 1963.
W.T. Stanbury, "The Legislative Development of Canadian Competition Policy," (1981) 2 Canadian Competition Policy Record 1.

[2] The MacQuarrie Report, supra, n.1.

B EARLY DEVELOPMENT OF THE LEGISLATIVE PROVISIONS TO 1950

The "godfather" of the present day legislation was an Act of the Parliament of Canada enacted in 1889, An Act for the Prevention and Suppression of Combinations formed in Restraint of Trade.[3] This Act, which was introduced one year before the Sherman Act[4] in the United States, was intended to be a codification of the common law. The text of section 1. of the Act read as follows:

> 1. Every person who conspires, combines, agrees or arranges with any other person, or with any railway, steamship, steamboat or transportation company, unlawfully,
>
> (a) to unduly limit the facilities for transporting, producing, manufacturing, supplying, storing or dealing in any article or commodity which may be a subject of trade or commerce; or

---

[3] An Act for the Prevention and Suppression of Combinations formed in Restraint of Trade, (1889), 52 Victoria, C41.

[4] Sherman Act, Act of July 2, 1890, C.647, 26 Stat. 209, as am.

> (b) to restrain or injure trade or commerce in relation to any such article or commodity; or
>
> (c) to unduly prevent, limit, or lessen the manufacture or production of any such article or commodity, or to unreasonably enhance the price thereof; or
>
> (d) to unduly prevent or lessen competition in the production, manufacture, purchase, barter, sale, transportation or supply of any such article or commodity, or in the price of insurance upon person or property,
>
> is guilty of a misdemeanor and liable, on conviction, to a penalty not exceeding four thousand dollars and not less than two hundred dollars, or to imprisonment for a term not exceeding two years; and if a corporation, is liable on conviction to a penalty not exceeding ten thousand dollars and not less than one thousand dollars.[3]

Subsequently to the first reading of the original version of the draft bill, the addition of the word "unlawfully" by the Banking Committee and the insertion of the words "unduly" and "unreasonably" by the Senate, rendered the section ineffectual. As Dr. L. Reynolds lamented:

> A more half-hearted statute can scarcely be imagined. Members of a combine could not be convicted unless the Crown proved that they were "unduly" doing something which was already unlawful at common law.[4]

The law reverted to the principles enunciated in the common law doctrines in restraint of trade.

The decision of His Honour Judge Dugas in the American

---

[3] 52 Vic, c. 41, S.1.

[4] Reynolds, L.G., , at p. 134.

Tobacco[7] case corroborates this deduction. The legislation in his view made no change in the common law and merely gave effect to the common law defence of "just cause". As Dugas J. concludes:

> [T]he bill proposed did not create a new law, but that it was simply the common law put into shape so as to let the public at large know the consequences of certain combinations or conspiracies forbidden by the common law.[8]

In 1892, the provisions of section 1 of the Act of 1889 were incorporated into the Criminal Code[9] as section 520. In the succeeding several years, frequent unsuccessful attempts were made to delete the words "unduly" and "unreasonably" from the Criminal Code.[10] A brief ray of hope for the Crown occurred in 1899 when the stultifying words were deleted.[11] However, both words were restored in 1900 as a further amendment[12] to the original Criminal Code. In 1906, S. 520 Criminal Code was renumbered S. 498. The prohibitions found both in the Act and the Criminal Code continued to be for all practical purposes ineffectual.

---

[7] See: infra, n. 9

[8] Ibid., at p. 457.

[9] Criminal Code, S.C. 1892, C. 29.

[10] Senator Read introduced a Bill in the Senate in 1894 to delete the words "unduly" and "unreasonably" from S.520 Criminal Code. It passed the Senate but only got as far as First Reading in the House of Commons. In 1895 and 1896 the Bill again failed to delete the offending words.

[11] Criminal Code Amendment Act, [1899], 62-63 Victoria, c.46.

[12] Criminal Code Amendment Act, [1900], 63-64 Victoria, c.46.

The first prosecution under the original proscription of 1889 was the *American Tobacco*[13] case which resulted in an acquittal. The first conviction arose out of the *R*. v. *Elliott*[14] case in 1903. A total of seven contested prosecutions were conducted during the period 1903 to 1910.[15] Five convictions were obtained. None of the cases, however, squarely addressed the growing problem of merger activity in Canada.

At the peak of the first merger wave, which occurred in 1910, William Lyon Mackenzie King, then Sir Wilfred Laurier's Minister of Labour, introduced the first Combines Investigation Act.[16] This Act attempted to remedy some of the shortcomings of its predecessors. Firstly, as a result of success with the tariff legislation,[17] a mechanism was incorporated for investigation whereby any six citizens could apply to the courts for an order directing an investigation. This legislation still failed to provide any continuity due to the fact that the boards of inquiry ceased to function once the inquiry was concluded. In addition, the legislation laid the cost of presenting the petition squarely in the hands of the complainants. However, this fledgling investigatory provision did develop eventually into the present section 7 of the new Competition Act.[18]

---

[13] *R* v. *American Tobacco of Canada* (1897), 3 Rev. de Jur. 453.

[14] *R*. v. *Elliott* (1905), 9 C.C.C. 505, 9 O.L.R. 648 (Ont.C.A.).

[15] Seven cases:
R. v. *Elliott* (1905), 9 C.C.C. 505, 9 O.L.R. 648 (Ont.C.A.).
R. v. *McGuire et al* (1906), 7 O.W.R. 225 (Ont.Prov.Ct.).
R. v. *Master Plumbers* (1907), 14 O.L.R. 295, 12 C.C.C. 371 (Ont.C.A.).
R. v. *McMichael* (1907), 10 O.W.R. 268, 18 C.C.C. 185 (Ont.H.C.J.).
R. v. *Grange* (1907), 6 W.L.R. 19, 13 C.C.C., 7 W.L.R. 564, 13 C.C.C. 428 (Man.C.A.).
R. v. *Clarke* (1907), 14 C.C.C. 46, 14 C.C.C. 57 (Alta.S.C.).
R. v. *Beckett et al* (1910), 20 O.L.R. 401, 15 C.C.C. 408 (Ont.H.Ct.).

[16] Combines Investigation Act, S.C. 1910, c. 37.

[17] Customs Tariff Act, S.C. 1897, c. 16.

Secondly, the definition of "combine" under the new Act was enunciated as follows:

> "Combine" means any contract, agreement, arrangement or combination which has, or is designed to have, the effect of increasing or fixing the price or rental of any article of trade or commerce or the cost of storage or transportation thereof, or of the restricting competition in or of controlling the production, manufacture, transportation, storage, sale, or supply thereof, to the detriment of consumers or producers of such article of trade or commerce, and includes the acquisition, leasing or otherwise taking over, or obtaining by any person to the end aforesaid, of any control over or interest in the business, or any portion of the business, of any other person, and also includes what is known as a trust, monopoly or merger.[19]

Two major changes were embodied in this definition. The definition of combine was to include what was known as a trust, monopoly or merger, thus paralleling section 2 of the

---

[18] Competition Act, S.C. 1986, proclaimed June 19, 1986. This Act was formerly Bill C-91.
[19] Supra, n.12.

Sherman Act. In addition, a combine was to be limited to those that were, or were designed to be, detrimental to consumers or producers. The new provisions did not however dampen the fires of merger activity at the turn of the century.

In 1919, the Combines Investigation Act of 1910 was repealed and replaced by the Board of Commerce Act,[20] which established a permanent tribunal to administer the provisions under its companion bill, the Combines and Fair Prices Act.[21] The Board was granted jurisdiction over investigation, permission for prosecution and adjudication in civil matters. It is instructive to note that the Board could, on its own initiative, commence an investigation under the Combines and Fair Prices Act. In 1921, both Acts were declared ultra vires the Federal Government, the court ruling that the two Acts permitted the Board to deal with cases on an individual basis, rather than to follow principles of general application. Thus, the Acts did not fall within the heads of either criminal law or trade and commerce, which were allocated exclusively to the Parliament of Canada.[22]

In 1923, the second Combines Investigation Act,[23] sponsored by King, now the Prime Minister, was enacted. This Act maintained the proscription against combines found in its predecessor Act and the Criminal Code. The primary contribution of this Act was to provide for a permanent administrator, the Registrar. Pursuant to the new Act, investigations could be initiated in three alternate ways: by formal application of six citizens, by the Registrar on his own initiative or on ministerial direction. With few alterations, the 1923 Act remained in force until the amendments of 1952.

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[20] Board of Commerce Act, S.C. 1919, c. 37.
[21] Combines and Fair Prices Act, S.C. 1919, c. 45.
[22] (1922), 1 A.C. 191; (1921), 60 D.L.R. 513.
[23] Combines Investigation Act, S.C. 1923, c. 9.

Several amending Acts were given royal assent and proclaimed in the interval preceding the extensive revisions of the early 1950's. In 1935, the responsibility for the administration of the Combines Investigation Act was transferred from the Department of Labour to the Minister responsible for the Department of Trade and Commerce.[24] In 1937, administration of the Act was delegated to a permanent Commissioner, replacing the former position of Registrar. Attempts at this early stage to include services in the Act and to provide separate definitions for merger and monopoly were eventually deleted from the Bill.[25] The administration of the Act was brought under the purview of the Minister of Justice in 1945, and amendments to the Act provided for the

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[24] Combines Investigation Amendment Act, S.C. 1935, c. 54.

[25] Combines Investigation Amendment Act, S.C. 1937, c. 23.

Commissioner to make studies on monopolistic conditions and report to the Minister.[26] This provision became the precursor to S.47 of the Combines Investigation Act respecting general inquiries. In 1949, two days after the scandal in which the Commissioner F.A. McGregor withheld the Flour Milling Report for ten months and felt compelled to resign, further amendments strengthened the enforcement of the Act.[27] First, there was a reaffirmation of the principle that documents found in the possession of individuals would be evidentiarily admissible (s. 45 Combines Investigation Act); secondly, prosecutions for combines offences would be tried by a judge without a jury.

The final amendments to the Act in this early era were recommended by the MacQuarrie Committee in the Interim Report on Resale Price Maintenance.[28] After a lengthy debate in the House of Commons, amendments were passed which prohibited resale price maintenance and refusal to deal by reason of resale price maintenance. The succession of these incremental improvements to the Combines Investigation Act acted as a springboard for the major scrutiny and overhaul in the early years of the next decade.

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[26] Combines Investigation Amendment Act, S.C. 1946, c. 44.

[27] Combines Investigation Amendment Act, S.C. 1949, c. 12.

[28] Supra, n.1; See also, M. Cohen et al., "The MacQuarrie Report and the Reform of Combines Legislation," (1952) 30 Canadian Bar Review 549.

C THE MACQUARRIE REPORT AND THE AMENDMENTS OF THE 1950'S

The final *Report of the Committee to Study Combines Legislation*[29] lead to fundamental changes to the Act[30] which, for the most part, remained an integral part of the legislation up to the enactment of the new Competition Act. The functions of the Commissioner were consequently bifurcated between two permanent bodies, the Director of Investigation and Research (DIR) and Restrictive Trade Practices Commission (RTPC). The Director was empowered with the responsibility of investigation and enforcement of the Act; the Commission was entrusted with the functions of appraisal and public reporting. Furthermore, the Act was amended in 1952 to provide for general enquiries into monopolistic situations or restraints of trade. Provisions were also made for obtaining an Order of Prohibition either as a sole remedy or in conjunction with other remedies. In addition, the prohibition orders were to be available after a Part V conviction (s.30(1) C.I.A.) as well as before the commission of an offence (s.30(2) C.I.A.). For the first time a structural remedy was available permitting the dissolution of a merger, trust or monopoly. The inclusion of these amendments marked the first time since the original Act of 1889 that a practical and workable structure was available to deal in a meaningful way with the complex legal and economic problems which arise in anticombines legislation. It was hoped that the authorities would now possess the requisite controls to prosecute offensive mergers.

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[29] *Ibid*.

[30] Combines Investigation Amendment Act, S.C. 1951, c. 30.

D THE LANDMARK DECISIONS OF THE 1960'S

For every flow, there is a ebb; in 1960 the government lost two important merger cases, the Canadian Breweries case[31] and the B.C. Sugar case.[32] In August of the same year, the Conservative government enacted several substantive changes to the Act.[33] The merger and monopoly offences were separated and the Criminal Code offences were incorporated into the Act. The Combines Branch was shifted to the new Department of Consumer and Corporate Affairs. The strength and practical relevance of the existing merger provisions were continually being queried and censured. It would not be for more than a decade before Parliament would attempt to close the floodgates left open by decisions rendered in the Canadian Breweries and B.C. Sugar cases.

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[31] R v. Canadian Breweries Ltd. (1960), 34 C.P.R. 179, 126 C.C.C. 133, [1960] O.R. 601 (Ont.H.Ct.). See also, J.C.H. Jones, "Mergers and Competition: The Brewing Case," (1967) 33 Canadian Journal of Economics & Political Science 551.

[32] R v. British Columbia Sugar Refining Co. Ltd. and B.C. Sugar Refinery Ltd. (1960), 38 C.P.R. 177, 129 C.C.C. 7, 32 W.W.R. 577 (Man.C.A.).

[33] Combines Investigation and Criminal Code Amendment Act, S.C. 1960, c.45; See also, E.D. Fulton, "New Amendments to the Combines Investigation Act," (1961) 61 Industrial Canada, 35; and L.A. Skeoch, "Combines Legislation, an Examination of Proposed Amendments," (1959) 66 Queen's Quarterly 87.

E THE INTERIM REPORT AND THE STAGE I AMENDMENTS

Rising out of the policy quagmire the Economic Council of Canada's Interim Report on Competition Policy,[34] published in 1969, formed the foundation upon which present day competition policy has been constructed. This report marked the commencement of a long and arduous march towards the goal of implementing meaningful reform of Canadian competition policy.[35] The Interim Report recommended a significant shift in the focus of competition policy: "We have put forward in this Report the view that the encouragement of economic efficiency should be the objective of Canadian competition policy, and it is accordingly in relation to this objective that the present legislation should be assessed."[36] The Council went on to recommend that mergers be evaluated on a cost-benefit basis by a new, civil law tribunal.

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[34] Economic Council of Canada, Interim Report on Competition Policy, Ottawa: Queen's Printer, 1969.

[35] See: C.H. Fulda, "Proposed Changes in Canadian Competition Legislation," (1970) 8 Osgood Hall Law Journal 415; J. Gillies, "A Review of the Economic Council's Interim Report on Competition Policy," Canadian Economic Policy Committee, 1969; D.H.W. Henry, "Mergers in Canada Under the Combines Investigation Act," (1969) 5 Texas International Law Forum 1; D.H.W. Henry, "Mergers, Rationalization, and Specialization Agreements," (1969) 8 Western Ontario Law Review 123; Bruce C. McDonald, "Canadian Competition Policy: Interim Report of the Economic Council of Canada," (1970) 15 Antitrust Bulletin 521; L.A. Skeoch, "The Case for Changes in Combines Law," (1966) 67 Industrial Canada 220; W.T. Stanbury, Business Interests and the Reform of Canadian Competition Policy, 1971-1975, Toronto: Carswell, 1977.

> In the sections that follow, we recommend that Canadian competition policy continue to retain certain broad prohibitions of price-fixing and closely related practices, misleading advertising, and resale price maintenance. The definition of these offences and of legal "defences" available to alleged offenders would be altered somewhat, but the offences would remain in a large measure per se and also minimal. All other matters of relevance for competition policy, including mergers and a wide range of trade practices, would become the responsibility of a new, civil law tribunal.[37]

Five broad probibitions were retained as per se offences: collusive arrangements to fix prices; collusive arrangements to allocate markets; collusive arrangements to prevent entry; resale price maintenance and misleading advertising. As a result of the particular assumptions governing industrial performance,[38] it was the judgment of the Council that none of the five offences was likely, "except possibly on rare and sporadic occasions, to result in appreciable public benefit.[39] In other words, only commercial practices and industrial structures which incontrovertibly precluded public advantage should be deterred. It is by now a well accepted axiom of *mainstream* economic thinking that mergers cannot *a priori* be branded in this manner.

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[36] Supra, n. 29, at 63.
[37] Ibid., at 100-101.
[38] Ibid., at 101.
[39] Ibid., at 102. See also: Kaysen, C. and Turner, D.F., Antitrust Policy, Cambridge: Harvard University Press, 1965, at pp. 142-160.

An extremely consequential viewpoint emerged from the *Interim Report* that has directed all subsequent legislative proposals. The Council recommended that merger law be placed on a civil law basis to be reviewed by a quasi-judicial administrative tribunal. It is not within the ambit of this paper to contemplate the constitutional validity of civil merger legislation; it was also not within the mandate of the *Interim Report*. The assumption is made that it is possible in the field of competition policy for the federal government to enact such provisions.[40] The Report mentions, in passing, two ways in which the federal government could enact civil controls: "The first way would be for the federal government to reach agreement with the provinces to make appropriate changes in the Constitution ... [t]he second ... to refer proposed legislation to the Supreme Court of Canada for the Court's opinion on its constitutional validity."[41] Parentically, the constitutional validity of legislation proposed seventeen years after the publication of the Interim Report has still not been unequivocably determined. The Combines Branch and the Department of Justice argue that the peace, order and good government clause, the trade and commerce powers grant the federal government jurisdiction to enact civil merger provisions reviewable by an administrative tribunal. The opposition parties and some special interest groups worry that the property and civil rights clause as well as those matters which are intra-provincial in nature will render the civil tribunal ultra vires. At the very least, many critics envision the constitutional issue being stalled in the courts for an indefinite period of time. Meanwhile, the entire attitude towards competition policy and mergers in particular may well have changed. Although every witness appearing before the Legislative Committee reviewing Bill C-91 voiced approval for mergers to be evaluated on a civil law basis, a majority of the members sitting on the committee openly echoed the call to eliminate the persistent ambiguity surrounding the constitutional validity of the civil tribunal.[42]

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[40] See: S.G.M. Grange, *The Constitutionality of Federal Intervention in the Market Place - The Competition Case*, Montreal: C.D. Howe Institute, 1975; Peter W. Hogg and Warren Grover, "The Constitutionality of the Competition Bill," (1976) 1 *Canadian Business Law Journal* 197.

[41] *Supra*, n. 29, at 107.

Criminal law has not been suited to the broad range of policy issues and implications that inherently accompany the public supervision of mergers. The inapplicability of criminal law in the area of mergers, and monopolization, has been the subject of theoretical discussion for several years:

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[42] Supra, n. 18.

> The present constitutional foundation for the Combines Investigation Act rests on the power of the Parliament of Canada to enact criminal law. This has contributed to the rigidity and inflexibility of the law and its administration. Criminal offences must be proved beyond a reasonable doubt. Charges must be expressed and proven in the categorical manner specified in the statute. The present provisions for injunctive proceedings against existing or proposed arrangements can only add limited flexibility because they must rest on the capacity of the Crown to meet the rigorous standards of criminal proof. Courts have no latitude to consider all the economic and commercial qualifications which might apply to particular cases and are compelled to adopt an "all or nothing" approach in deciding whether offences have been committed. In addition, the classification of commercial arrangements as criminal has created a bad psychological background for administration, which, as early as 1910, was recognized by Mackenzie King and has undoubtedly militated against wholehearted acceptance of the legislation by the business community.[43]

The Council incorporated these concepts into a triumvirate of reasons to shift merger law to civil procedure:

> The basic reasons for seeking to place some of the federal government's competition policy on a civil law basis would be to improve its relevance to economic goals, its effectiveness, and its acceptability to the general public. The greater flexibility afforded by civil law is especially to be desired in those areas of the policy that do not lend themselves well to relatively unqualified prohibitions and that may in addition call for some case-by-case consideration of the likely economic effects of particular business structures or practices.[44]

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[43] D. Gordon Blair, "Combines: The Continuing Dilemma," in Lang, O.E. (ed.), Contemporary Problems of Public Law in Canada, Toronto: University of Toronto Press, 1968.

[44] *Supra*, n. 29, at 109.

There exist two types of civil procedures. One sets standards which do not prohibit a merger until it is reviewed by the adjudicative body and determined to be undesirable. Similar in nature to the reviewable trade practices under Part IV.1 of the Combines Investigation Act, 1976, these civil procedures do not prohibit mergers until a prohibition order is granted. The other form of civil procedure prohibits mergers but without criminal sanctions, a form of civil penal code. The only remedy in this case is a permanent injunction or dissolution order.

In conjunction with shifting merger control to the civil area, the Interim Report endorsed the formation of a specialized tribunal, the Competitive Practices Tribunal. The Tribunal would retain some of the characteristics of a court, such as the observance of the rules of natural justice, while proceeding in a less formal manner. The functions of the Tribunal would, like an ordinary court, encompass the hearing and adjudication of issues as well as the imposition of remedies. The tribunal would, in addition, absorb the functions of the Restrictive Trade Practices Commission. "[The Tribunal] would engage in economic analysis and in the issuance of reports similar to many of those now issued by the Restrictive Trade Practices Commission so that the important process of public education, the documentation of particular cases or inquiries, and the formulation of recommendations thereon would be continued."[43] The Tribunal composed of as many as seven members from a blend of qualified backgrounds, would be charged with the following principal functions:

(1) examine certain corporate mergers to determine whether any such mergers were on balance not in the public interest, and in cases where they were judged to be not in the public interest, impose or recommend appropriate remedies;

(2) examine certain types of proposed intercompany agreements respecting exports and the specialization of production to determine whether the agreements were on balance in the public interest, and in cases where they were judged to be in the public interest, place the agreements in a public register and designate them as "registered" export or specialization agreements;

(3) examined the employment of certain trade practices to determine whether such employment was on balance not in the public interest, and in cases where it was judged to be not in the public interest, impose or recommend appropriate remedies; and

(4) sponsor general inquiries similar in character to those now provided for in Section 42 of the Combines Investigation Act, and report on such inquiries.[44]

With respect to the substantive merger provisions, the recommendations of the Council submitted that "certain" mergers were to be scrutinized by the Competitive Practices Tribunal on a social cost-benefit basis. The Interim Report lacked specificity on which mergers were to be screened;

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[43] Ibid., at 110.
[44] Ibid., at 112.

however, the Interim Report gave first formal credence to the proposition that mergers could be procompetitive, or at least neutral, as well as anticompetitive. The role of the Competitive Practices Tribunal would be "to examine those mergers that appeared to contain a significant potential for harm, ..."[47] [emphasis added]. This statement is often quoted to substantiate a de minimus defence. The primary test in examining a merger would be, "whether the merger was likely to lessen competition to the detriment of final consumers, and whether there were likely to be any offsetting public benefits."[48] The Tribunal would also be "requested" to pay attention to the following check list of relevant matters that described the competitive nature of the market in which the merger developed, in so far as they would affect "substantial economic performance"[49]:

(1) the degree of effective control over the acquired firm or firms that the merger conferred upon the acquiring individual or firm (in assessing effective control, the tribunal would be expected to look not only to the size of the purchase but also to such matters as the composition of the board of directors of the acquired company, if this seemed relevant);

(2) the history of previous acquisitions by the acquired and acquiring firms and by other firms within the affected industry or industries;

(3) the shares of relevant markets held by the

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[47] Ibid., at 114.
[48] Ibid., at 115-116.
[49] Ibid., at 116.

acquired and acquiring firms;

(4) the amount and intensity of domestic and import competition in relevant markets;

(5) the situation, both before and after the merger, regarding financial and other barriers to the entry of new competitors into the relevant markets;

(6) the likelihood that an acquired firm, had it continued its separate existence, would have been a vigorous and effective competitor in relevant markets;

(7) the existence of possible alternative buyers of the acquired firm or firms; and

(8) the likelihood that the merger would be productive of substantial "social savings", i.e., savings in the use of resources (including resources used for such purposes as research and development), viewed from the standpoint of the Canadian economy as a whole.[50]

It will become apparent to the discerning reader that the proposed amendments to the Combines Investigation Act in the subsequent two decades, commencing with Bill C-256 and culminating with Bill C-91 in 1985, all found their fundamental structural genesis for reviewing mergers in the proposed test and relevant criteria enunciated in the Interim Report.

The Economic Council made little effort to distinguish between horizontal, vertical and conglomerate mergers. In reference to conglomerate mergers, the Interim Report mentions, "There is relatively little experience of them and even less analysis of their nature and modes of operation."[51] This passing disinterest in conglomerate mergers stands in sharp contrast to the contemporary view of merger activity.

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[50] Ibid.

The Interim Report presented, as the primary goal of the Department of Consumer and Corporate Affairs, the advancement of the consumer interests. "The dominant underlying theme of the present Report has been the desirability of directing competition policy towards the maximization of economic efficiency, real income and consumer welfare."[52] This goal was to be achieved by setting the twin target variables of prevention and deterrence. It was hoped that the Competitive Practices Tribunal would, in fact, achieve these target variables through enforcement techniques that would emphasize publicity and compliance. The following remark by the Council places its Report in perspective. "As a form of social control of industry, well-working competitive markets supported by competition policy are remarkably cheap by comparison with alternatives such as direct regulation."[53]

Finally, almost as a passing thought, the Council ponders the use of a registration procedure to ensure the timely consideration of all significant mergers. This concept has certainly been expanded in the years that followed to include consideration of the inclusion of pre-clearance procedures and pre-notification requirements.

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[51] Ibid., at 118.
[52] Ibid., at 184.
[53] Ibid., at 193.

In June of 1971, the government moved on the recommendations set forth in the Interim Report by introducing Bill C-256,[54] the proposed Competition Act, which unfortunately met with vigorous disapproval from the business community.[55] The bill was allowed to die on the Order Paper.

In July, 1973, Mr. Herb Gray, Minister of Consumer and

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[54] Bill 256, "An Act to Promote Competition, to provide for the general regulation of trade and commerce, to promote honest and fair dealing, to establish a Competitive Practices Tribunal and the Office of the Commissioner, to repeal the Combines Investigation Act and to make consequential amendments to the Bank Act." First Reading: June 29, 1971, 3rd Session, Twenty-Eighth Parliament, 19-20 Eliz. II, 1970-71 [The Competition Act].

[55] For a discussion of Bill C-256, see: Canada, Department of Consumer and Corporate Affairs, The Competition Act: Explanatory Notes, Ottawa: Supply & Services, 1971; Conference Board of Canada, Canada's Competition Policy , Ottawa: The Conference Board of Canada, 1972; Milton Moore, How Much Price Competition? The Prerequisites of an Effective Canadian Competition Policy, Montreal: McGill-Queen's Press, 1970; R.S. Nozick, "Recent Proposals in Antitrust Law," Unpublished LL.M. thesis, Harvard University, 1972; L.A. Skeoch, (ed.), Canadian Competition Policy, Kingston: Queen's University, Industrial Relations Centre, 1972; W.T. Stanbury, Business Interests and the Reform of Canadian Competition Policy, 1971-1975, Toronto: Carswell, 1977, at Chapter 7.

Corporate Affairs as he then was, announced that the government would split its competition policy proposals into two stages: the first stage to deal with the widely accepted amendments to the Combines Investigation Act and the second stage to formulate policy on the more contentious areas of conspiracies, monopolies and mergers. On November 6, 1973, Bill C-227,[54] was given first reading in Parliament. Following two additional drafts of Bill C-227, the Stage I amendments became law, effective January 3, 1976.[57] Among the important changes incorporated into the Combines Investigation Act were the following:

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[54] Bill C-227, "An Act to amend the Combines Investigation Act and the Bank Act to amend an Act to amend the Combines Investigation Act and the Criminal Code," First reading, November 5, 1973, First Session, Twenty-Ninth Parliament, 21-22 Elizabeth II, 1973.

1. Services were brought under the Act (S.2 Combines Investigation Act);
2. Part IV.1, civilly reviewable trade practices were established;
3. The Restrictive Trade Practices Tribunal was given the jurisdiction to deal with the civilly reviewable trade practices (Part IV.1 Combines Investigation Act);
4. Private, civil, single damage actions were incorporated (S. 31.1 Combines Investigation Act).

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[57] For a discussion of the development and evaluation of the Stage I amendments, see: C.W. Borgsdorf, "The Virtually Unconstrained Legal Environment for Mergers in Canada," (1973) 18 *Antitrust Bulletin* 809; Canada, Department of Consumer and Corporate Affairs, *Proposals for a New Competition Policy for Canada, First Stage, 1973*, Ottawa: Supply & Services, 1973; "Proposals for a New Competition Policy for Canada, First Stage, 1973," (1974) 19 *Antitrust Bulletin* 13; Canada, House of Commons Standing Committee on Finance, Trade and Economic Affairs, *Proposals for Change*, Ottawa: Supply & Services, 1977; Gordon Kaiser, "The Stage I Amendments: An Overview," (1976) 1 *Canadian Business Law Journal* 147; Bruce C. McDonald, "Reviewable Marketing Practices in Canada," (1977) 20 *Antitrust Bulletin* 801; D.G. McFetridge, "The Emergence of a Canadian Merger Policy: The Erco Case," (1974) 19 *Antritrust Bulletin* 1; William P. McKeown, "How the Conspiracy Provisions of the New Competition Law Affect the Professions and Services," (1977) 2 *Canadian Business Law Journal* 4; David McQueen, "Competition Policy in Stages: Recent Developments in Canada," (1976) 20 *Antitrust Bulletin* 751; David L. McQueen, "Tribunals and Take-Overs in Canada," *Canada's Competition Policy*, The Conference Board of Canada, Ottawa, 1972; L.A. Skeoch, "Merger Issues in Canada," (1971) 16 *Antitrust Bulletin* 131; and L.A. Skeoch, "The Rationale for New Directors in Policy," (1972) 17 *Antitrust Bulletin* 629.

F THE STAGE II AMENDMENTS

The Stage II amendments to the Combines Investigation Act were preceded by not only some unfavourable political machinations over the "judges affair" involving the then Minister of Consumer and Corporate Affairs, Andre Ouellet,[58] but also some perspicatious studies relating to the controversial issues in merger policy.[59] The emerging forerunner of the research during this period has become known as the *Skeoch-McDonald Report*.[60] Prepared by an economist and a lawyer, in consultation with Messrs. Belanger, Bronstein and Twaits, the Report proposed a transfer of the legal procedure from criminal to civil: "Criminal law, its procedures and its remedies cannot be made realistic for mergers..."[61] The authors were firmly of the view that the Restrictive Trade Practices Commission should be discontinued. In its place, the authors envisage the "National Markets Board," to which the government would appoint highly qualified, non-political appointees.

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[58] Mr. Ouellet was a member of the Legislative Committee overseeing the Second Reading committee stage of Bill C-91.

[59] See: R.I. Cohen, and J.S. Ziegel, The Political and Constitutional Basis of a New Trade Practices Act, Ottawa: Information Canada, 1976; R.J. Bertrand, "The Combines Investigation Act: What Does Competition Mean?," (1977)4 Canadian Business Review 45; Peter W. Hogg and Warren Grover, "The Constitutionality of the Competition Bill," (1976) 1 Canadian Business Law Journal 197; Robert S. Nozick, "The Regulation of Price Discrimination Under the Combines Investigation Act," (1976) 54 Canadian Business Review 390; W.T. Stanbury, "Penalties and Remedies Under the Combines Investigation Act, 1889-1976," (1976) 14 Osgoode Hall Law Journal 571; M.J. Trebilcock et al., Proposed Policy Directions for the Reform of the Regulation of Unfair Trade Practices in Canada, Ottawa: Information Canada, 1976; Jennifer Whybrow, "The Case for Class Actions in Canadian Competition Policy: An Economist's Viewpoint," in A Proposal for Class Actions Under Competition Policy Legislation, Ottawa: Information Canada, 1976; and Neil J. Williams, "Damages Class Action Under the Combines Investigation Act," in A Proposal for Class Actions Under Competition Policy Legislation, Ottawa: Information Canada, 1976.

> It is almost trite that on specialized subjects good experts are better than courts but bad experts can be much worse. We should stress that we place more faith in experience and informed common sense than in cloistered "expertise". The responsibilities we propose for the Board are formidable but we are confident that if the matter of appointments to the Board is treated as seriously by the government as are appointments to judicial office, we will have a Board capable of making perceptive and realistic decisions and making the statute work to the long-run benefit of the country. If, however, the government in making the appointments were to be influenced by any grounds other than

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[60] L.A. Skeoch and B.C. McDonald *et al.*, *Dynamic Change and Accountability in a Canadian Market Economy*, Ottawa: Supply and Services Canada, 1976; L.A. Skeoch, "The Dynamic change Report and the Proposed Competition Act," in J.R.S. Pritchard, W.T. Stanbury, and W.T. Wilson, (eds.), *Canadian Competition Policy: Essays in Law and Economics*, Toronto: Butterworths, 1979; L.A. Skeoch and B.C. McDonald, "Dynamic Change and Accountability in a Canadian Market Economy," *Annual Report of the Director of Investigation and Research*, Appendix VI, Ottawa: Supply and Services Canada, 1976; and W.T. Stanbury, "Dynamic Change and Accountability in a Canadian Market Economy: Summary and Critique," (1977) 15 *Osgoode Hall Law Journal* 1.

[61] *Ibid.*, p. 292; see also, p. 313.

> personal qualifications for the job, the results could be considerably more damaging than leaving the law as it is.
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> The importance of this recommendation cannot be overstated. It is the crux of our proposals concerning administration and adjudication and is central to the success of most of the substantive proposals.[42]

The Report initiated discussions on a registration procedure, advance rulings, interim injunctions and the failing company defence, all of which have been incorporated in one form or another in the new Competition Act. The Report concluded that the primary thrust of competition policy should be the long term encouragement of technological, organizational and managerial change to enhance and preserve a dynamic, economic environment. In order to accomplish this objective, the Report recommended the elimination of protected positions in all sectors of the economy in an attempt to promote adaptability and flexibility throughout the economy. This outlook foreshadows the Chicago School and Landes and Postner views on entry barriers discussed in Chapter IX of this paper. The essence of the report was to place heavy reliance on the market system. The strategic elements involved in promoting such dynamic adaptability in Canada were summarized in the following three elements:

1. the prohibition of artificial restraints, that is, restraints not based on superior

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[42] Ibid., p. 295.

economic performance;

2. government assuming much of the heavy cost of economic change rather than encouraging resistance to change by protectionist devices; and,

3. if necessary, the alteration of the environmental circumstances by upgrading incentives and strengthening pressures for adjustment so that questions of innovation, economies of scale, specialization of firms, rate of economic growth, and the like, could be largely left to dynamic, market-like arrangements.[43]

The authors of the Report emphasize that the problem with applying a general rule to a specific case is that it produces more governmental intervention than is envisioned to be acceptable at the outset. The authors propose that, "The preferred approach is to identify the artificial restraints that control or inhibit dynamic change and to fashion environmental changes that will restore so far as possible marketlike arrangements and pressures - and stop the intervention at that point."[44]

The Skeoch-McDonald Report, as well as the accompanying and spinoff studies undertaken following the introduction of the Stage I amendments, led to the introduction in March,

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[43] L.A. Skeoch, "The Dynamic Change Report and the Proposed Competition Act," in J.R.S. Pritchard, W.T. Standbury, and W.T. Wilson, (eds.), Canadian Competition Policy: Essays in Law and Economics, Toronto: Butterworths, 1979, p. 81.

[44] Ibid., p. 81.

1977, of Bill C-42.[45] This Bill was withdrawn by the Minister of Consumer and Corporate Affairs, Anthony Abbott, in less than one month.[46] November of the same year, Warren Allmand, the new Minister, introduced the second version of the Stage II amendments in the form of Bill C-13.[47] A highlighted summary of Bill C-13 would necessarily emphasize the following:

1. The Statute contained a set of competition policy objectives;

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[45] Bill C-42, "An Act to amend the Combines Investigation Act and to amend the Bank Act and other Acts in relation thereto or in consequence thereof," First reading: March 16, 1977, Second Session, Thirtieth Parliament, 25-26 Elizabeth II, 1976-77.

[46] For a more complete analysis of the Stage II Amendments, including both Bill C-42 and its younger sibling, Bill C-13, see: Canada Department of Consumer and Corporate Affairs, *Proposals for a New Competition Policy for Canada, Second State*, Ottawa: Supply & Services, 1977; J.R.S. Pritchard, W.T. Stanbury and W.T. Wilson (eds.), *Canadian Competition Policy: Essays in Law and Economics*, Toronto: Butterworths, 1979; Law Society of Upper Canada, *New Combines Legislation*, Toronto: Osgoode Hall, January, 1977; M.T. MacCrimmon and W.T. Stanbury, "Policy Death by Administrative Restriction: The House Committee's Report on Bill C-42, The Competition Act of 1977," (1977) 15 *Osgoode Hall Law Journal* 485; G.B. Reschenthaler and W.T. Stanbury, "A Clarification of Canadian Merger Policy," (1977) 22 *Antitrust Bulletin* 673; Martin J. Rochwerg, "Proposed Stage II Amendments to Canadian Combines Legislation - Bill C-42," (1977) 15 *Osgoode Hall Law Journal* 51; J.W. Rowley and W.T. Stanbury, *Competition Policy in Canada: Stage II, Bill C-13*, Montreal: Institute for Research on Public Policy, 1978.

[47] Bill C-13, "An Act to amend the Combines Investigation Act and to amend the Bank Act and other Acts in relation thereto or in consequence thereof," First reading: November 18, 1977, Third Session, Thirtieth Parliament, 26 Elizabeth II, 1977.

2. Merger and monopoly offences were transformed from criminal to civil law;
3. The test for unlawful mergers was altered;[48]
4. A quasi-judicial tribunal was established to be called the Competition Board, to review civilly reviewable trade practices;
5. Class actions for civil damages were included, and
6. Alterations to administration and enforcement under the Combines Investigation Act, especially its relationship to the Foreign Investment Review Act, were addressed.

Bill C-13 died on the Order Paper, 10 October, 1978, an outcome that was beginning to become all too familiar.

G THE REPORT OF THE ROYAL COMMISSION ON CORPORATE CONCENTRATION AND THE THIRD IMPRESSION OF THE STAGE II AMENDMENTS

No new bills were released until April 1984. In the interim, two substantial reports and one Department discussion paper were promulgated. In May of 1978, the first report, the Report of the Royal Commission on Corporate

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[48] Ibid., S.31.71.

Concentration,[69] was released accompanied by 33 research studies (See: Bibliography). The underlying current of public policy in the Royal Commission Report eroded the economic significance of merger activity:

> "that competition was not seriously threatened by corporate mergers, and also that the costs of a review process by the Competition Board were not justified by the unsatisfactory results that may be expected from it. ...It is not that a process requiring a prediction of the economic effects of mergers cannot be made to work; it is that the process can operate only at what we think will be a prohibitive cost and that the results of the process will not be significantly worthwhile."[70]

The second study, referred to as the Bertrand Report,[71] was a voluminous and comprehensive insight into the oligopolistic behaviour of the "seven sisters" in the petroleum industry. Although a thorough understanding of the

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[69] Canada, Report of the Royal Commission on Corporate Concentration, Ottawa: Supply and Services Canada, 1978. For instructive reviews of the Report see: Steve Globerman, "The Report of the Royal Commission on Corporate Concentration and its Implications for Competition Policy," in Canadian Competition Policy, by J.R.S. Pritchard, W.T. Stanbury, and T.A. Wilson (eds.), Toronto: Butterworths, 1979; Paul K. Gorecki, The Administration and Enforcement of Competition Policy in Canada: 1960-1975, Research Monograph No. 6, Bureau of Competition Policy, Consumer and Corporate Affairs Canada, Ottawa: Supply and Services Canada, 1979; Paul K. Gorecki and W.T. Stanbury (eds.), Perspectives on the Royal Commission on Corporate Concentration, Toronto: Butterworths, 1979; In addition, a complete list of the background papers may be found in the bibliography to this paper. "Background Papers to the Report of the Royal Commission on Corporate Concentration."

[70] Ibid., at p. 166.

[71] Bertrand Report: Director of Investigation and Research, "The State of Competition in the Petroleum Industry", Ottawa: Supply and Services Canada, 1981.

structure and conduct of firms in a dominant position is gained from a perusal of the Bertrand Report, not much new insight is added to the merger issues. The third widely circulated musing on competition policy was the Department's "questionnaire" circulated to the business and academic community as the 1981 Proposals.[13] The 1981 Proposals segmented competition policy into ten component parts and queried the public on contentious policy issues. The basic structure of the 1981 Proposals is outlined below:

1. Adjudication of the Proposed New Law.
2. The Problem with Existing Merger Law and Proposals for Reform.
3. The Problem with Existing Monopoly Law and Proposals for Reform.
4. The Problem with the Existing Statutory Monopoly Provisions and Proposal for Reform.
5. Export and Import Restrictions by Multinational Enterprises.
6. The Problem with the Existing Conspiracy Law and Proposal for Reform.
7. Specialization Agreements.
8. Ban on Participation in International Cartels.
9. Systematic Delivered Pricing Proposals.
10. Transfer of Responsibility for Competition Policy in Banking from the Bank Act to the

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[13] Canada, Department of Consumer and Corporate Affairs, Proposals for Amending the Combines Investigation Act: A Framework for Discussion, Ottawa: Supply and Services Canada, 1981.

Combines Investigation Act."[73]

At the time, it was expected that a new bill incorporating the proposals outlined above would be introduced sometime in early 1982. Not surprisingly, the next bill was not tabled until April, 1984.

The 1981 Proposals were designed to query the business, academic and government community on twenty-one specific questions on which the Department of Consumer and Corporate Affairs anxiously awaited public input. The following is a selective list of questions relevant to a discussion on mergers:

> 1. Do you favour the use of the regular courts over reliance on an administrative board or tribunal for the adjudication of the non-criminal provisions of the Act?[74]
>
> 2. In the review of mergers, would you prefer the introduction of a market-share threshold as a means of assuring greater certainty in the application of the law to an approach which relies on a balancing of the likely costs and benefits of proposed mergers?
>
> 3. At what level do you believe the market-share threshold should be set in percentage terms, to ensure that significant anticompetitive mergers would be prevented while at the same time ensuring that mergers necessary to the development of fully efficient Canadian enterprises would not be inhibited thereby? In other words, from a public policy viewpoint, where should the balance be struck in terms of a

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[73] Ibid.

[74] Ibid., at p. 3.

> specified market-share firms could acquire via acquisition of competitors?
>
> 4. In the case of very large and complex mergers and acquisitions by extremely large firms, where a public policy case for requiring pre-notification as set out above is justifiable, what in your opinion should be the threshold in terms of millions of dollars of assets or sales at which firmst should be required to pre-notify acquisitions of competitors, customers or suppliers (e.g., $100, $300, $500 million)?'[75]

The 1981 Proposals reiterated the need to shift merger law from criminal to civil jurisdiction. However, the 1981 Proposals reverted to the use of the courts not an expert quasi-judicial tribunal in contradistinction to earlier Bills. The major test to determine unlawfulness required proof of a significant lessening of actual or potential competition. In addition, for greater certainty in cases involving relatively large acquisitions, an irrebuttable presumption would deem mergers over a specified market share threshold as significantly lessening competition. Interestingly enough, the 1981 Proposals deleted the availability of the economies defence. These proposals met with severe criticism from all quarters, not the least of which arose from the vociferous business lobby groups, known informally at the time as the "Gang of Three": the Business Council on National Issues, the Canadian Manufacturers' Association and the Canadian Chamber of Commerce. In April of 1983, the proposed amendments to the Combines Investigation Act were delayed until the fall. In August of the following year, the Honourable Judy Erola became the Minister of the Department of Consumer and Corporate Affairs and fostered the negotiation style of consultative legislative development. In December, 1983, the Speech from the Throne promised new competition legislation. As a result of the consultative process among government, business and academics, the Department of Consumer and Corporate Affairs drafted three proposed bills. These bills were never made public. It was not until April of 1984 that a draft proposal in the form of Bill C-29[74] was revealed to the public.

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[75] Ibid., at p. 8.

Bill C-29, the last Bill to be introduced by the Liberals, was in fact the third version of Stage II amendments to the former Combines Investigation Act. In terms of substantive provisions, Bill C-29 would again transfer merger law to civil law to be adjudicated by the courts. Proposed mergers could be prohibited and consummated mergers could be dissolved where the merger lessened competition significantly. However, in contrast to the 1981 Proposals, an absolute efficiency defence was available where the merger brought about substantial real net savings of resources to the Canadian economy. In addition, for large mergers in which post merger assets or sales exceeded $500 million, the parties were required to pre-notify the Director of Investigation and Research and provide him with certain pertinent information. The primary goal of Bill C-29 was to strengthen competition policy by emphasizing efficiency as the primary objective of competition policy. The bill died on the Order Paper on 9 July, 1984, when the House of Commons rose for a general election.

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[74] Bill C-29, "An Act the Amend the Combines Investigation Act and the Bank Act and Other Acts, in consequence thereof," First Reading: April 2, 1984, Second Session, Thirty-second Parliament, 32-33 Eliz. II, 1983-84.

H THE PROGRESSIVE CONSERVATIVE PROPOSALS

On 20 March, 1985, the new Conservative Minister of Consumer and Corporate Affairs, Michel Cote, released his department's Consultation Paper[77] on reforming the competition policy in Canada. The Paper outlined four distinct areas of concern to the new government:

1. Adjudication:

   The competition policy legislation should be shifted to civil law economic tribunal. Such a tribunal should act only in a judicial capacity; the administrative and investigatory functions of the Restrictive Trade Practices Commission should be entirely transferred to the Director of Investigation and Research.

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[77] Canada, Consumer and Corporate Affairs, Reform of Competition Policy in Canada: A Consultation Paper, Ottawa: Supply and Services, 1985.

2. Investigatory Powers:

The four powers of the Director of Investigation and Research to search premises, seize documents, subpoena witnesses and require information and documents must be molded to the protections under S.10 of the Charter of Rights and Freedoms.

3. Mergers:

The paper outlined three specific issues related to mergers: the lessening of competition substantially test, the efficiency test and the status of joint ventures.

4. Pre-notification:

Simply stated, the Consultation Paper supported a less complex mechanism for notifying the Director of Investigation and Research of proposed mergers.

In an address to the MacDonald-Cartier Club, in Calgary, on April 26, 1985, the Honourable Michel Cote previewed his general "game plan" for reforming the Canadian competition policy:

> First, we have the move towards less onerous and less burdensome regulation. Second, we have a growing recognition of the importance of freer trade and trade

enhancement.[78]

In an effort to emphasize the importance he placed on an economic tribunal, Mr. Cote stated that, "I must confess that, unless persuaded otherwise, I am personally inclined to favour the expert tribunal approach."[79] As well as reassuring the western audience that joint ventures would be afforded special attention, the Minister went to some length to indicate that the forthcoming premerger notification requirements would "be significantly simpler in their formulation than previous proposals."[80] Mr. Cote addressed the constitutional issues which had arisen subsequent to the enactment of the Canadian Charter of Rights and Freedoms:

> Our proposals for the investigative powers in the Act will strike a delicate balance between the rights of individuals as guaranteed by the Charter on the one hand, and the government's need to be able to effectively enforce the Act, on the other.[81]

In conclusion, the speech highlighted the fundamental philosophy which would be embodied in any legislation subsequential to Bill C-29:

> I think that competition policy should be viewed as a vital part of economic policy itelf, rather than as a system of regulatory constraints. Indeed, if the Combines Act is effective, and markets work well, there will be less need for direct government intervention.

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[78] Canada, Consumer and Corporate Affairs, Canadian Competition Policy: A New Director, Speech by the Hon. M. Cote, Calgary, April 26, 1985.

[79] Ibid., at p. 7.

[80] Ibid. Upon viewing the prenotification provisions in the Competition Act, one must one why the Minister reached this conclusion. See: Chapter VI, infra.

[81] Ibid.

> It strikes me as unfortunate that we do not always recognize the importance of competition policy legislation in protecting the free functioning of the market economy.[12]

The Department of Consumer and Corporate Affairs continued to make substantial efforts to reform Canadian competition policy. Consultation continued, and in August of the same year the Macdonald Report[13] on the state of the Canadian economy further accelerated the process. The substance of the Report was to emphasize the beneficial effect on competition and ultimately social welfare by tearing down international trade barriers and deregulating otherwise competitive markets.

From the date of the Minister of Consumer and Corporate Affairs' speech in April to the announcement that a fourth bill to reform competition policy would be tabled in Parliament, the many observers speculated on which proposals the legislation would adopt. In the 5 October, 1986, Financial Post, the headline on page 13 predicted: "Big Mergers That Will Fight Imports To Get Green Light." Negotiations had been held all summer long between the Department of Consumer and Corporate Affairs and the expanded "Gang of Five."[44] The indication was that, after years of business-government turmoil over modernizing competition law, a politically saleable balance between the interests of business, both large and small, and consumers had been reached. The Minister of Consumer and Corporate Affairs struck an Advisory Council of respected businessmen, lawyers and academics from the private sector to refine the Department's proposals. In addition, the subject of competition policy was discussed at the Federal-Province meetings of the Minister of Consumer and Corporate Affairs and his provincial counterparts. On 17 December, 1985, the Minister of Consumer and Corporate Affairs tabled a new and long-awaited competition bill, Bill C-91, which was heralded as the reconciliation of the diverse perspectives on merger policy. The Globe and Mail, in an article by Christopher Waddell,[45] 18 December, 1985, indicated that the new bill borrowed much from the Macdonald Report on the country's economic prospects. Mr. Waddell expressed the view that, "The theme running throughout the proposed changes is that competition policy must be brought in line with Canada's role in the international trading world." Mr. Giles Gherson, in a front page article in the the 28 December, 1985, edition of the Financial Post, entitled "Reigning In Mergers," described the proposals as a tougher, state-of-the-art competition regime. However, Mr. Gherson adds parenthetically, "There are lots of ifs and buts scattered through the mergers and abuse of dominant position sections of Cote's bill that will undoubtedly supply a field day for combines lawyers."[46] The business community, led by the "Gang of Five", had lobbied vociferously that the onus of proof in any merger test should be with the Crown to show that no substantial competition remained. Mr. Cote refused such a test, arguing that the merger provisions would be severely impeded as a result.

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[12] Ibid., at p. 8.

[13] Canada, Report of the Royal Commission on the Economic Union and Development Prospects for Canada, D.S. Macdonald, Chairman, Ottawa: Supply and Services Canada, 1985.

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[44] The Gang of Five are: CCC, CMA, CBA, BCNI, CFIB.
[45] Globe and Mail, December 18, 1985.

On 9 June, 1986, Bill C-91 was given Third Reading in the House of Commons; on 16 June, the Bill was given Royal Assent and on 19 June Bill C-91 was finally proclaimed as the Competition Act.

The objective of this paper is to discover whether the new merger provisions reflect the government's express intentions to guarantee more restrictive proscriptions. Mr. Gherson's article, supra, concluded on a note of uncertainty:

> Warns William Rowley, a partner at the Toronto law firm, McMillan Binch, and a competition law expert who has advised major business associations on competition law reform: "Business and consumers alike now face a period of uncertainty about the new law. Like the constitution when it was introduced, the fact that Canada will have a new competition law, a new quasi-

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[46] Financial Post, " Reigning in Mergers," December 28, 1985, at p. 2.

> judicial tribunal to adjudicate it, and a new director of combines to bring forward cases means a genie is being unleashed and it will take a while to know what it all means."[87]

This uncertainty is one this paper will endeavour to dispel.

The discoveries may not be as expected.

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[87] Ibid.

III ADJUDICATION

A CRIMINAL V. CIVIL PROCEDURE

On 19 June, 1986, Bill C-91,[1] a Bill to create the Competition Act and the Competition Tribunal, was proclaimed as law, with great expectations in business and government circles that the new legislation will be a great improvement over the former Combines Investigation Act. Bill C-91 was divided into four Parts:

1. Part I: Competition Tribunal Act;
2. Part II: Competition Act (formerly the Combines Investigation Act, 1976);
3. Part III: Consequential Amendments;
4. Part IV: Transitional and Coming Into Force Amendments.

The government is confident that the new provisions will set up a clear and understandable, yet effective, framework of "rules of the game" to ensure that markets will perform their primary purpose of allocating resources efficiently.

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[1] To facilitate reference, the following abbreviated citations will be used throughout the remainder of the paper without reference to their corresponding formal legal citation: Combines Investigation Act; *Interim Report*; Bill C-256; Bill C-256; Bill C-227; *Skeoch-McDonald Report*; Bill C-42; Bill C-13; *Royal Commission Report*; *1981 Proposals*; Bill C-29; *1985 Consultation Paper*; *Macdonald Report*; Bill C-91; Competition Tribunal Act; Competition Act. Formal references may be found in the Bibliography.

Hanging as a spectre over the new Act is the affirmation in its accompanying Guide that the government's new Act is consistent with the reliance on free market forces advocated in the Macdonald Report:

> In its Report the Commissioners recommended placing greater reliance on market forces to fuel a sustained recovery and economic growth. They also recognized that competitive markets reduce the need for direct government intervention and regulation. The Commissioners went on to say that it is in the ultimate interests of all Canadian to reform Canada's outmoded competition policy and it made recommendations consistent with the amendments being proposed by the Government.[3]

The new Act provides a comprehensive administrative mechanism to circumvent the difficulties that had accumulated over the years respecting the adjudicative procedures provided in the Combines Investigation Act. As a result of years and years of intense debate and lobbying over the state of the then prevailing provisions in the Combines Investigation Act, issues such as the proper forum to be employed, the Tribunal's composition, the matter of judicial review and appeal, constitutionality, as well as Cabinet override, were all thoroughly canvassed and addressed in the Competition Act.

Under the former Act, the merger sanctions contained in section 33 Combines Investigation Act, created an indictable offence, punishable on conviction by an unlimited fine or imprisonment for two years. Since the publication of the Interim Report, all commentaries and proposed legislative changes have unequivocally recommended a transfer of the merger proscriptions from criminal to civil procedure. The onerous and near impossible task of proving anticompetitive economic effects on a burden of proof beyond a reasonable doubt has long been accepted as unworkable and inappropriate for evaluating potentially harmful mergers.

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[3] Canada. Department of Consumer and Corporate Affairs, Competition Law Amendments: A Guide, Ottawa: Supply and Services Canada, 1985.

In addition, a criminal prosecution was conceptually inappropriate to deal with the complex balancing of economic issues that must be accomplished in any attempt to analyze the incidence of merger activity on anticompetitive conduct and allocative efficiency. Finally, the stigma of a criminal conviction on firms, whose raison d'etre has always been to conquer the competitor, seemed misguided and ill-suited. As the Economic Council of Canada in the Interim Report expounded:

> The basic reasons for seeking to place some of the federal government's competition policy on a civil law basis would be to improve its relevance to economic goals, its effectiveness, and its acceptability to the general public. The greater flexibility afforded by civil law is especially to be desired in those areas of the policy that do not lend themselves well to relatively unqualified prohibitions and that may in addition call for some case-by-case consideration of the likely economic effects of particular business structures or practices. The unsuitability of criminal

law in such areas has been well described as follows:[3] Bill C-256 incorporated such modifications, but, as stated early, this intitial attempt to amend the Combines Investigation Act (1976) died a silent death on the Order Paper.

The Skeoch-McDonald Report also counselled that the merger provisions be evaluated on "reasonable probabilities"[4] by transforming the merger provisions from criminal to civil jurisdiction:

> The recommendations made in this report would, if implemented, result in transferring certain areas of substantive law from the criminal courts to the civil jurisdiction of the National Markets Board. Criminal remedies would, however, remain an important support for the competition laws. Types of conduct that are widely viewed as being contrary to the public interest regardless of their particular factual context, and which can be defined with reasonable specificity in advance so as to give fair warning, would be prohibited by criminal law. This would include failure to comply with Board orders which will be reviewable by the courts as to the degree of their specificity.[5]

Again, Bill C-42[6] and Bill C-13[7] implemented the basic proposals exhorted throughout by their mother report, the Skeoch-McDonald Report.

By 1978 and the publication of the Report of the Royal Commission on Corporate Concentration, it was well accepted in both business and government circles alike, that troublesome mergers should be dealt with according to substantive civil procedure. Both the 1981 Proposals[8] and Bill C-29[9] structured the test for non-permissible mergers in civil terms.

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[3] Interim Report, p. 109.
[4] Skeoch-McDonald Report, p. 89.
[5] Ibid., p. 316.
[6] Bill C-42, S.31.71.
[7] Bill C-13, SS.16, 16.5.

In an example of consistency which endures in no other area of the history of competition policy amendments, the Competition Act and its precusor, the 1985 Consultation Paper, persisted in transforming the merger provisions to civil law:

> There is general agreement that competition policy issues involving mergers, monopolies and other related matters should not be dealt with by criminal sanctions, but should be governed instead through the process of civil law.[10]

Section 64(1) Competition Act grants the Competition Tribunal authority to adjudicate Part VII reviewable matters which would include mergers, consequently codifying what has been recognized since the Interim Report as an incontrovertible principle of merger legislation. The civil burden of proof on the preponderance of evidence is the one amendment to the former Combines Investigation Act which will undeniably afford the Department of Consumer and Corporate Affairs a greater opportunity to enjoin perceived offensive mergers.

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[8] 1981 Proposals, note 18.

[9] Bill C-29, S.31.72.

[10] 1985 Consultation Paper, n.4 at p. 1.

B COURT V. QUASI-JUDICIAL TRIBUNAL

1. NEED FOR REFORM

(a) The Constitutional Controversy

One of the high profile debates that has accompanied the progress of competition proposals over the years has been the controversy regarding the appropriate forum in front of which to hear and adjudicate lengthy and complex merger cases. Two related topics arise if one opts, as the new Act has, for the tribunal approach. First, how should the board be constituted and secondly, what is the constitutional status of such a tribunal?

In outline form, the argument in favour of the use of the courts stresses the certainty and continuity of judicial decisions. Furthermore, the judgements of the courts allow full rights of appeal. Also, lawyers and businesspeople are familiar with the courts and, given past history, may expect more favourable decisions. In stark contrast, the proponents of a tribunal emphasize that there are inherent complexities embodied in the substantive proscriptions that would necessitate an adjudicative body expertly trained and continually confronted with such issues. In addition, the flexibility and informality available before a quasi-judicial body would be more effective in dealing with the nature of the economic questions being tackled.

The former Combines Investigation Act[11] created dual responsibilities of investigation and research under the Director of Investigation and Research[12] and consideration and report under the Restrictive Trade Practices Commission.[13] From a theoretically sound constitutional perspective, the Director of Investigation and Research should be compartmentalized into an exclusively administrative and investigatory role. The accuser should not also play the role of the adjudicator. And conversely, the Restrictive Trade Practices Commission[14] should not be entrusted with any jurisdiction concurrently relegated to the Director of Investigation and Research under Part I[15] of the present Act.[16] The Restrictive Trade Practices Commission, upon ex parte application of the Director, could, under the old Act,[17] compel witnesses to be examined[18] and documents to be produced.[19] Furthermore, the Commission could review and report on statements of evidence,[20] as well as authorize investigatory powers.[21] As noted above, the Restrictive Trade Practices Commission could also require the Director of Investigation and Research to enter into a S.47 general inquiry under the present Act. These powers created at least the appearance that the R.T.P.C. was not completely unbiased and neutral.

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[11] Combines Investigation Act, S.C. 1978 c.-23, as am. Any subsequent reference to the Acts or Bills wil imply reference to citations supplied in footnote 1, supra.

[12] Ibid., S.5.

[13] Ibid., S.16.

[14] Subsequent references to the Restrictive Trade Practices Commission shall refer to the Restrictive Trade Practices Commission constituted pursuant to S.16 Combines Investigation Act (1976).

[15] Combines Investigation Act, 1976, s. 8.

[16] Competition Act.

[17] Combines Investigation Act, 1976.

[18] Combines Investigation Act, s. 17(1).

[19] Ibid., S.17(4).

In the Southam[22] case, the Supreme Court of Canada decided under the Canadian Charter of Rights and Freedoms[23] that these powers of the Restrictive Trade Practices Commission pursuant to section 10 of the former Act, which were of an investigatory nature and which created even the perception of prejudice, would impair its ability to act as an impartial tribunal and were therefore unconstitutional. These constitutional difficulties are discussed infra, in chapter IV.

(b) The Composition Of The Adjudicative Body

Prior to the enactment of the Competition Act much discussion centred on whether the appropriate court would be the Federal Court, the superior courts of the provinces or some specially constructed entity. Once the Honourable Michel Cote revealed his preference towards a quasi-judicial tribunal, the debate was focused on the constitution of the board. On the one side, advocates of judicial members argued that judges would be impartial, versed in the law and trained in dispute resolution. The proponents of expert members emphasized that the issues arising under the new Act would be complex and would require considerable expertise. This controversy was solved creatively in the Competition Act.

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[20] Ibid., S.18.

[21] See the following Chapter IV, Investigations, of this paper for a review of the constitutional issues surrounding this subject.

[22] Hunter et al. v. Southam Inc. (1984), 14 C.C.C. (3d) 97 (S.C.C.).

[23] Part I of the Constitution Act 1982, Schedule B of the Canada Act (U.K.).

2. RECENT PROPOSALS FOR REFORM

The former Act conferred on the courts[24] jurisdiction to hear offences under the illegal merger sections contained in Part V. The Economic Council of Canada, in its Interim Report, submitted two alternate possibilities: first, special judges of the Federal Court-Trial Division could be earmarked for competition cases; second, a specialized "Competitive Practices Tribunal" could be established to absorb the functions of the Restrictive Trade Practices Commission. The fundamental impetus for such a recommendation was to ensure specialized knowledge and expertise in the adjudicators who were required to resolve complex economic issues. Although the Interim Report contemplated a specialized administrative tribunal to avoid in the future, what were perceived by many legal experts to have been conflicting and unintelligible common law judgments, there was no attempt to sever the administrative and adjudicative functions of the Commission.

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[24] Any S.33, Combines Investigation Act (1976), illegal merger offence may have been tried in a superior court of criminal jurisdiction (S.44(2) Combines Investigation Act (1976)), or with consent of the accused, in the Federal Court-Trial Division (S.46(2) Combines Investigation Act (1976)).

> As will be seen, the body that we propose would, like any ordinary civil court, carry out functions of hearing, adjudication and the imposition of remedies. In addition, however, it would engage in economic analysis and in the issuance of reports similar to many of those now issued by the Restrictive Trade Practices Commission so that the important process of public education, the documentation of particular cases or inquiries, and the formulation of recommendations thereon would be continued. The new tribunal would absorb the functions and perhaps also some of the qualified personnel of the Restrictive Trade Practices Commission.[25]

The recommendations of the Interim Report were embodied in Bill C-256. Although the merger provisions would have been reviewed by the "Competitive Practices Tribunal"[26] rather than the courts, the tribunal assumed all the existing powers of the Restrictive Trade Practices Commission. The Director of Investigation and Research would have maintained his authority under the Combines Investigation Act, but would simply have been renamed the "Commissioner".[27]

The Stage I amendments were mute on this contentious issue. It was not until the Skeoch-McDonald Report[28] that a recommendation surfaced to eliminate the Restrictive Trade Practices Commission and replace it with a more neutral administrative tribunal, the "National Markets Board".[29] It was contemplated by the authors of the report that the "National Markets Board" would be entirely independent and autonomous; a decade ago the authors foresaw the difficulties of overlapping administrative and quasi-judicial functions:

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[25] Interim Report, p. 110.
[26] Bill C-256, S.3. The Tribunal was to replace the R.T.P.C.
[27] Ibid., S.11.

> It is fundamental that persons with these powers exercise them in complete independence and on the basis of evidence submitted to them by the parties as assessed in the light of their own general experience and knowledge. The specialized body we propose is a substitute for the regular courts and is not a regulatory agency in the American tradition of having legislative, adjudicative and executive functions rolled into one and the same body such as is the case, for example, with the Federal Trade Commission. Accordingly, we propose that the Board not have the power to initiate proceedings, have no capacity or responsibility for general research into economic matters or types of practices, not engage in general rule-making and be completely removed from the criminal law functions performed by the Bureau of Competition Policy and the courts.[30]

The recommendations of the Skeoch-McDonald Report were assimilated into Bill C-42 and its finely tuned cousin, Bill C-13. Bill C-42 established the Competition Policy Advocate[31] to replace the Director of Investigation and Research. The Competition Policy Advocate was to conduct an inquiry on its own intiative, or on request from the Minister of Consumer and Corporate Affairs, but not on request of the Competition Board.[32] Unfortunately, the Competition Board was still empowered to conduct inquiries of a general nature into monopolistic situations, thus jurisdiction still crossed over the line of acceptable adjudicative functions. Section 17 of Bill C-42 authorized the naming of a Hearing Officer, who would not be a member of the Board, to preside over the hearing of evidence. Bill C-13 modified the procedure somewhat by deleting the requirement of an *ex parte* preliminary application by the Competition Policy Advocate to prove before the Board to prove that a *prima facie* case existed.[33]

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[28] Skeoch-McDonald Report, p. 289.
[29] Ibid., p. 293.
[30] Ibid., p. 298-9.
[31] Bill C-42, S.5(1).

The third major drive to amend the adjudicative procedures commenced with the *1981 Proposals for Reform*.[34] Exemplifying the desultory mood of the policy advisors, the *1981 Proposals for Reform* recommended that the courts, not a selective tribunal, be authorized to hear and review merger offences.[35] The decision on whether the federal or provincial courts should be utilized was left to a future date. Bill C-29 incorporated this view in section 31.72 by requiring the Director of Investigation and Research to apply to the "court" for review of an unlawful merger situation.

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[32] *Ibid*., S.47.
[33] *Bill* C-13, S.31.91(1).
[34] The Report of the Royal Commission on Corporate Concentration was silent on this point.
[35] *1981 Proposals*, note 7, p. 18.

The pendulum motion of public policy from the courts to a tribunal and back was not disrupted by the Conservative Minister of Consumer and Corporate Affairs in his 1985 Consultation Paper.[36] To foreshadow the reversal in advance, the Macdonald Report reiterated the demand in the 1985 Consultation Paper for such a tribunal.[37] To the surprise of very few observers, Bill C-91 moved in the opposite direction to that taken by Bill C-29. However, to manage the concerns associated with the constitution and constitutionality of the tribunal, the Bill for the first time created an entirely separate act in order to ensure an independent, adjudicative "Competition Tribunal" which could decide the merger issues outlined in Part II of the Bill. These provisions remained unaltered in the Competition Tribunal Act.

3. THE COMPETITION TRIBUNAL ACT

Part I of Bill C-91 was actually a companion Act to the Competition Act, established to set up the "Competition Tribunal".[38] The Restrictive Trade Practices Commission was struck[39] and replaced by a hybrid tribunal composed of not more than four judges from the Federal Court-Trial Division, appointed by Cabinet on recommendation of the Minister of Justice, and not more than eight other members, again appointed by the Governor in Council but recommended by the Minister of Consumer and Corporate Affairs.[40] It is hoped that such a diverse expert tribunal will meld together the legal expertise required as well as the business and economic acumen necessary to make informed and reasoned judgments in complex economic situations.[41] Pursuant to section 8, the Competition Tribunal has jurisdiction to hear all applications made under Part VII of the Competition Act,[42] which would include the new merger provisions. The Competition Tribunal is a court of record, empowered to deal with matters informally, expeditiously as well as fairly,[43] and imbued with all the rights and privileges to examine witnesses and documents that are vested in a superior court of record.[44] Questions of law will be determined by the judicial members; questions of fact or law and fact will be reviewed by all the members.[45]

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[36] 1985 Consultation Paper, note 10; For a concise summary of the pros and cons of an expert tribunal, see notes 5 to 9.

[37] Macdonald Report, p. 223.

[38] Competition Tribunal Act, s. 3(1).

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[39] Ibid., s. 20(1).

[40] Ibid., s. 3(2).

[41] For a discussion of the basic issues in the ongoing controversy between the use of the courts and a specialized tribunal, see: William Grover, "The Competition Bill: The Courts or a Specialized Administrative Tribunal," in J. Robert S. Pritchard, W.T. Stanbury, and T.A. Wilson (eds.) Canadian Competition Policy: Essays in Law and Economics, Toronto: Butterworth's, 1979, p. 97.

[42] Part VII, is subsumed under Part II of Bill C-91, and contains all civilly reviewable matters, including mergers.

[43] Competition Tribunal Act, s. 9.

The separation of functions between the Director and the Competition Tribunal will prima facie eliminate the problem of the overlapping investigatory and adjudicative mandates which the Southam case strongly criticized and prohibited. The Competition Act ensures that the Competition Tribunal's functions will be entirely adjudicative:

> It will have no role in supervising the investigative powers of the Director, initiating investigations or providing research of policy advice to the Government. As a result, section 47 of the present Act, which permits research inquiries, will be repealed. In the future, should situations arise where research inquiries into the state of competition in a particular industry are necessary, the Government can rely on the general provisions of the Inquiries Act for creation of an ad hoc Commission of Inquiry.[46]

The authority which accompanied the Restrictive Trade Practices Commission's S.47 general inquiry powers has been eliminated, as well as its jurisdiction to review evidence and examine witnesses. The elimination of the general inquiry powers was unnecessary; they could have been transferred to the Director.[47] As the Guide to Bill C-91 concluded:

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[44] Ibid., s. 8(2).
[45] Ibid., s. 12.
[46] Supra, n.2, at p. 11.
[47] This suggestion is attributed to Professor R. Nozick, Faculty of Law, University of Alberta.

> The issue of adjudication of competition matters has been the subject of much discussion over the long history of competition law reform. Many interested parties have proposed reliance on the ordinary courts to adjudicate competition matters. One factor often cited in support of the courts is their ability to produce consistent results with clear and full rights of appeal. Others have expressed a preference for the use of a specialized tribunal because it would provide greater potential for expertise in economics and business, and would permit more scope for response by the decision maker to social and economic change. In particular, lay experts are better able to reflect the reality of the business world.
>
> On balance, the Government believes it is more appropriate that these matters be adjudicated by a highly judicialized tribunal. This hybrid will allow the use of expert lay persons as well as judges in the decision-making process. Nevertheless, the Government agrees that it is very important to have in the law an adjudication system that ensures the impartiality, due process and certainty which is associated with the courts.[48]

However, the question of the constitutional validity of the Tribunal itself as a federally delegated administrative body still remains as a potentially lethal snare. It is inevitable that the constitutionality of the Competition Tribunal Act will be tested in the courts; the resultant effect will be to render ineffectual the entire Competition Act while the issue is being decided.[49]

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[48] Supra, n.2, at p. 10.

[49] It is not the objective of this paper to research the constitutional status of the proposed tribunal. However, it must be emphasized that this issue lay heavily on the minds of the members of the Legislative Committee in Second Reading of Bill C-91. It is certainly, at the very least, an area of research imploring further study.

Section 3(2) of the Competition Tribunal Act establishes that the constitution of the "Competition Tribunal" shall consist of two classes of members, judicial members and other members. There is a great danger that a hierarchy will develop between the two groups. Only the judicial members have the right to determine all matters, whether of law or fact; whereas, the lay members may determine only matters of fact or mixed law and fact. The chairman of the tribunal must be chosen from the judicial members. Although the tenure of both groups shall not exceed seven years, it is likely that the judges will carry on the day-to-day determination of tribunal matters, while the other members will be called upon from time to time as the need arises. The possible outcome could be an elevation of the judicial members to first class members while the other members could be relegated to second class associates. This is in spite of the fact that both types can be appointed on a full-time basis. As an offsetting argument, due to the fact that a majority of the substantive provisions in Part VII of the Competition Act appear to be solely matters of mixed fact and law, the part-time members will be crucial to the decision making process.[18]

In regard to appeals from decisions of the Tribunal, all appeals lie to the Federal Court of Appeal as if the decision or order were a judgment of the Federal Court-Trial Division.[11] Caution has been raised in some quarters that under the Rules governing the Federal Court of Canada, a trial de novo may be available. Such an opportunity on appeal would obviously circumvent the primary objective of preferring the expert tribunal over the courts in the first place. It may be advisable to explicitly prohibit a retrial or new trial on the merits particularly in the light of section 13(2) of the Competition Tribunal Act. Section 13(2) Competition Tribunal Act allows appeal on a matter of fact only with leave of the Federal Court of Appeal:

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[18] Competition Tribunal Act, S.12.

> (2) An appeal on a question of fact lies under subsection (1) only with the leave of the Federal Court of Appeal.

Section 27 of the Federal Court Act, S.C. 1970-71-72, c. 1, grants jurisdiction to the Federal Court of Appeal to hear appeals from the Trial Division, consequently, pursuant to S. 13(1) Competition Tribunal Act, from the Tribunal. Section 28 FCA permits the Court of Appeal to review non-administrative decisions of on a quasi-judicial body. Along with S.18 FCA, the Court of Appeal is endowed thrice with powers to open up the Tribunal's decision. The foregoing notwithstanding, there does not appear in the Federal Court Act an express right to appeal on the facts. Therefore, the fears expressed below by Mr. Ouellet and Mr. Hunter are not well-founded:

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[11] Ibid., S.13.

> Mr. Ouellet: There is the feeling that the appeal to the Federal Court could be not only on question of law and question of law in fact, but could also be on question of fact, and that is something that in the course of ordinary case court does not exist.
>
> . . .
>
> My question is does this legislation give the right to appeal on question of fact?
>
> Mr. Hunter: Yes, I think it does. (See: House of Commons, Minutes of Proceedings of Legislative Committee, May 12, 1986, at p. 7:34.)

Finally, pursuant to section 16 of the Competition Tribunal Act, the Tribunal may make general rules for regulating the practice of the Tribunal, these rules being subject to the approval of Cabinet. Many of these regulations may have spillover effects into the substantive law areas; consequently, it is suggested that a mandatory publication and hearing procedure be imposed on the tribunal before the proposed rules can be submitted to Cabinet for final approval.

The matter of the availability of a Cabinet override has developed in the last few years into a hotly debated aspect of merger policy. The alternatives available and their ramifications will be discussed in greater detail in Chapters VII (Injunctions) and IX (Conglomerate Mergers); however, it must be pointed out at this juncture that the new Competition Tribunal Act contains no provisions for Governor in Council review or override. This omission is in sharp contrast to the intentions voiced in the 1985

Consultation Paper which preceded and formed the basis for the present Act. The structure of large mergers is changing; the majority are of the non-horizontal or "pure" conglomerate type. To date, no practical objective economic means has been developed to assess these forms of mergers. Perhaps, on a purely economic basis these mergers cannot be anticompetitive or detrimental to social welfare. However, they may be adverse to the broader concept of the "public interest". Consequently, these political issues should be resolved by politicians, in Cabinet.

IV INVESTIGATION

A THE NEED FOR REFORM

The Combines Investigation Act, (1976), conferred three general and wideranging investigatory powers on the Restrictive Trade Practices Commission:

1. The required submission of pertinent information;
2. General Search and Seize powers;
3. The compulsion of witnesses, and the production of documents.

Pursuant to section 9(1) Combines Investigation Act, the Director of Investigation and Research was empowered to require a written return under oath showing in detail the full disclosure of any information "touching or concerning" the business. The Director of Investigation and Reseach received his authorization from the Restrictive Trade Practices Commission:

> 9.(2) The Director shall not issue a notice under subsection (1) unless, on the _ex parte_ application of the Director, a member of the Commission certifies, as such member may, that such notice may be issued to the person or officer of a corporation disclosed in the application.[1]

The entry of premises and the seizure of any relevant evidence was governed by section 10 of the former Act. Again the Director of Investigation and Research was under a duty to apply to the Commission:

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[1] Combines Investigation Act (1976), S.9(2).

> 10.(3) Before exercising the power conferred by subsection (1), the Director or his representative shall produce a certificate from a member of the Commission, which may be granted on the ex parte application of the Director, authorizing the exercise of such power.[2]

Lastly, the Commission exceeded its adjudicative role by being involved in the decision to compel witnesses to give evidence, either by way of affidavit, or by parole evidence. Again, the Director had to apply to the Commission for certification to require evidence upon affidavit:

> 12.(1) The Director may, by notice in writing, require evidence upon affidavit or written affirmation, in every case in which it seems to him proper to do so, but the Director shall not so require unless, on the ex parte application of the Director, a member of the Commission certifies, as such member may, that the Director may make such a requirement to the person disclosed in the application.[3]

Section 17 of the former Act placed the burden on the Director to satisfy the Restrictive Trade Practices Commission, ex parte, that a person should be examined under oath or that documents should be seized:

> 17.(1) On ex parte application of the Director, or on his own motion, a member of the Commission may order that any person resident or present in Canada be examined upon oath before, or make production of books, papers, records or other documents to such member or before or to any other person named for the purpose by the order of such member and may make such orders as seem to him to be proper for securing the attendance of such witness and his examination, and the production by him of books, papers, records or other documents and may otherwise exercise, for the enforcement of such

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[2] Ibid., S.10(3).
[3] Ibid., S.12(1).

> orders or punishment for disobedience thereof, all powers that are exercised by any superior court in Canada for the enforcement of subpooenas to witnesses or punishment of disobedience thereof.[4]

The effective enforcement of competition legislation requires a very delicate and tenuous balancing procedure. On the one hand, the detection of merger activity before consummation is complex and difficult at the best of times. Business conduct, which may potentially be in contravention of the Act, is usually very sophisticated, complex, and clandestine. Furthermore, the information that is required tends to be of a hypothetical nature involving issues expressed in terms of potentials and likelihoods. On the other hand, individual rights, which have been recently codified in the Canadian Charter of Rights and Freedoms,[5] must not be limited unless demonstrably justified. Recent decisions of the Supreme Court of Canada underscore these countervailing objectives.

In Hunter v. Southam, the Supreme Court of Canada decided the issue in favour of protecting individual rights under the Charter. The Charter declares that, unless restrictions are demonstrably justifiable, the following legal rights are inviolate:

8. Everyone has the right to be secure against

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[4] Ibid., S.17(1).

[5] Part I of the Constitution Act 1982, Schedule B of the Canada Act (U.K.).

unreasonable search and seizure.[6]

In the Southam[7] case, the Supreme Court of Canada declared that at least the following three requirements must be satisfied for a search to be "reasonable":

1. A valid search requires a warrant granted by an impartial adjudicator;
2. The investigating officers must have reasonable and probable grounds to believe that an offence has been committed, and
3. The investigating officers must have reasonable and probable grounds to believe that relevant evidence is on the premises.

Applying these criteria, the Court declared the search and seizure powers under S.10 Combines Investigation Act to be inconsistent with the legal rights guaranteed in the Charter. Only the second of the three conditions was satisfied. The requirement that the warrant be issued by an impartial adjudicator was breached because the body which granted the warrant (RTPC) was also obligated to investigate the offence; at least the perception of bias in favour of granting the warrant existed. The third requirement was also not satisfied because the former Act did not specify what standard of proof was required. Dickson C.J. overtuned lower court decisions which applied a post facto analysis of section 8 of the Charter. The purpose of the section was to protect the individual from unreasonable state intervention. Section 10 of the Act was inconsistent with this objective.

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[6] Ibid. at S.8.

[7] Hunter et al. v. Southam Inc. (1984), 14 C.C.C. (3d) 97 (S.C.C.); See also: Skis Rossignol Canada Ltd. et al. v. Lawson A.W. Hunter et al., 11 January, 1985, Federal Court-Trial Division, T-2812-84; Re Weigel and the Queen (1983), 7 C.C.C. (3d) 81.

The subpoena powers were held in question in two recent cases, the NHL' case and the Business Forms' case. The constitutional validity of S.17 of the former Act were considered but not held to be invalid. Consequently, there existed tremendous momentum to amend the investigatory powers in the Combines Investigation Act to render them consistent with the rights guaranteed under the Canadian Charter of Rights and Freedoms.

B THE NEW PROVISIONS UNDER THE COMPETITION ACT

The new provisions rectify the inherent inadequacies which have developed since 17 April, 1982. In general, all three of the major investigatory powers are vested in the Director of Investigation and Research, not the Restrictive Trade Practices Commission, and are subject to supervision by the courts. The authority to compel witnesses to testify

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' Zeigler et al. v. Hunter et al., [1984] 2 F.C. 608 (Fed.C.A.); leave to appeal refused 8 March, 1984.

' Crain et al. v. Couture and RTPC (1984), 6 D.L.R. (4th) 478 (Sask.Q.B.); See also the judgement of Lysyk J. referenced at (1984) 68 B.C.L.R. 32.

under oath, produce documents or supply detailed written information may be delegated to a "presiding officer" upon application by the Director to the courts, not the Tribunal:

> 9.(1) Where, on the ex parte application of the Director or his authorized representative, a judge of a superior or county court or of the Federal Court is satisfied by information on oath or affirmation that an inquiry is being made under section 8 and that any person has or is likely to have information that is relevant to the inquiry, the judge may order that person to
>
> (a) attend as specified in the order and be examined on oath or affirmation by the Director or his authorized representative on any matter that is relevant to the inquiry before a person, in this section and sections 10 to 12 referred to as a "presiding officer", designated in the order;
> (b) produce a record, or any other thing, specified in the order to the Director or his authorized representative within a time and at a place specified in the order; or
> (c) make and deliver to the Director or his authorized representative, within a time specified in the order, a written return under oath or affirmation showing in detail such information as is by the order required.[10]

The search and seize provisions, previously contained in section 10 of the Combines Investigation Act, have been expanded and modified in an attempt to conform with the Chater. They require the Director of Investigation and Research to satisfy the courts that he has reasonable and probable grounds to believe that a person has contravened the merger provisions and that relevant records are situated on the premises:

> 13.(1) Where, on the ex parte application of the Director or his authorized representative, a judge of a

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[10] Competition Act, S.9(1).

> superior or county court or of the Federal Court is satisfied by information on oath or affirmation
>
> (a) that there are reasonable grounds to believe that
> (i) a person has contravened or failed to comply with an order made pursuant to section 29, 29.1 or 30, or Part VII,
> (ii) grounds exist for the making of an order under Part VII, or
> (iii) an offence under Part V or VI has been or is about to be committed, and
> (b) that there are reasonable grounds to believe that there is, on any premises, any record or other thing that will afford evidence with respect to the circumstances referred to in subparagraph (a)(i),(ii) or (iii), as the case may be,
> the judge may issue a warrant under his hand authorizing the Director or any other person named in the warrant to
> (c) enter the premises, subject to such conditions as may be specified in the warrant, and
> (d) search the premises for any such record or other thing and copy it or seize it for examination or copying.''[11]

Protection of the confidentiality[12] of inquiries and solicitor-client privilege[13] complete and unify the new provisions governing the investigatory powers of the Director of Investigation and Research. Presuming that certain classes of mergers should be subject to state review, the provisions of the Competition Act will diminish the lingering constitutional conflicts which have been subject to recent disparaging pronouncements in the courts. However, the doubts may continue.

Even if one were to recommend the abolition of the substantive merger review provisions enacted in Section 64, it might well be desirable to retain similar investigatory powers in the hands of the Director of Investigation and Research for use in Cabinet consideration. The former Act authorized search and seizure powers under the Inquiries Act.[14] Due to the deletion of the Director's powers available pursuant to the Inquiries Act, non-compliance by the merging parties under the pre-notification provisions might necessitate search, seizure and examination capabilities consistent with those contained in the Competition Act.

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[11] Ibid., S.13(1).
[12] Ibid., S.16.
[13] Ibid., S.17.

Finally, concern has been raised that the search and seizure powers under the new Act will be declared unconstitutional, notwithstanding all the amendments specifically tailored to avoid this result. The concern arises because the substantive provisions under section 64 are structured as reviewable practices under Part VII, not offences of the Clayton Act variety. As a consequence, there is no unlawfulness accompanying any merger until the Tribunal reviews the section 64 application and declares a contravention of the Act. Any warrants issued prior to this finding would not be substantiated on the belief, with reasonable and probable grounds, that an offence had been committed; rather, a warrant under s.13(1) Competition Act would be presumed constitutionally reasonable. Otherwise, the second criterion required by the Supreme Court of Canada in *Southam* would not be satisfied. The Department's rebuttal may rely on Dickson C.J.'s *dicta* in the *Southam* case. His Lordship acknowledged that a search could be upheld as reasonable in certain situations, but the Crown would be required to prove that the search was constitutionally reasonable. As Dickson C.J. states:

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[14] These powers were previously available to the Director under S.21 Combines Investigation Act, 1976.

> Here also, the decision in *Katz*, *supra*, is relevant. In *United States* v. *Rabinowitz*, 339 U.S. 56 (1950), the Supreme Court of the United States had held that a search without warrant was not *ipso facto* unreasonable. Seventeen years later, however, in *Katz*, Stewart J. concluded that a warrantless search was *prima facie* "unreasonable" under the Fourth Amendment. The terms of the Fourth Amendment are not identical to those of s. 8 and American decisions can be transplanted to the Canadian context only with the greatest caution. Nevertheless, I would in the present instance respectfully adopt Stewart J.'s formulation as equally applicable to the concept of "unreasonableness" under s. 8, and would require the party seeking to justify a warrantless search to rebut this presumption of unreasonableness.[15]

Although the Director would apply for a warrant under s.8 Competition Act, the same argument of constitutional reasonableness would be applicable to overcome any difficulty arising from the lack of an offence being committed. Besides, the Director need only show that a reviewable practice "is likely" to occur. Undoubtedly this issue will end up in the Supreme Court of Canada.

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[15] *Southam*, *supra*, n. 57, at p. 161.

V THE SUBSTANTIVE TEST FOR MERGERS UNDER THE COMPETITION ACT

A DEVELOPMENT OF THE LEGISLATION

1. INTRODUCTION

In an effort to compile and distill the diverse array of factors which have been proposed or adopted to categorize the lawfulness of a merger or proposed merger, the following four topics will be used to structure the discussion:[1]

(1) Definition of a merger,

(2) The substantive test,

(3) Remedies available, and

(4) Exemptions.

Although admittedly not in precise detail the overview presented of the substantive test will highlight the types of mergers scrutinized, the form of the test employed having regard to the structure-conduct-performance paradigm[2] and the specific criteria involved. The latter observations will strive to review any additional factors which the adjudicative body has been directed to consider, including the intent of the merging parties and the burden of proof to be applied. Due to their alleged importance in Canadian competition policy, efficiencies as a defence have been severed from the general comments on exemptions and incorporated into the remarks respecting the substantive test.

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[1] For a comprehensive list of the many elements which have been considered, see Appendix A.

[2] See: F.M. Scherer, Industrial Market Structure and Economic Performance, Chicago: Rand-McNally, 1970.

2. DEFINITION OF A MERGER

The nascent provision respecting mergers in the Act of 1889 made no mention of mergers explicitly; rather, a "combine" which unduly lessened competition was proscribed.[3] It was not until 1910 that the term "combine" was defined as any contract, agreement, arrangement or combination which restricted competition to the detriment of consumers or producers.[4] The definition of a combine included the merger of separate commercial entities.

The first explicit recognition of mergers in Canadian competition legislation occurred in the short-lived Combines and Fair Prices Act[5] of 1919. The expression was deemed to include "mergers, trusts and monopolies, so called" which operated or were likely to operate "to the detriment or against the interest of the public, consumers, producers or others."[6] It is apparent to the casual student of the recently repealed Combines Investigation Act, 1976, that this early standard characterizing illegal mergers has survived right up to the enactment of the new Competition

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[3] See: Chapter II, section B, supra, for the full text of the original provision.

[4] Ibid.

[5] Combines and Fair Practices Act, 9-10 Geo. 5, c. 45; S.C. 1919.

[6] Ibid., at s. 2.

Act 1986. This initial definition was refined in the Combines Investigation Act, 1923,[7] and retained through subsequent amending statutes until the next major revision of the Combines Investigation Act came in 1952. The 1923 version stated in part that competition had to be lessened to the public detriment.[8]

> In this Act, unless the contract otherwise requires,
>
> 1. combines which have operated or are likely to operate to the detriment or against the interest of the public, whether consumers, producers or others, and which
> (a) are mergers, trusts or monopolies, so called; or
> (b) result from the purchase, lease, or other acquisition by any person of any control over or interest in the whole or part of the business of any other person; or
> (c) result from any actual or tacit contract, agreement, arrangement, or combination which has or is designed to have the effect of
> I limiting facilities for transporting, producing, manufacturing, supplying, storing or dealing, or
> II preventing, limiting or lessening manufacture or production, or
> III fixing a common price or resale price or a common rental, or a common cost of storage or transportation, or
> IV enhancing the price, rental or cost of article, rental, storage or transportation
> V preventing or lessening competition in, or substantially controlling within any particular area or district generally, production, manufacturer, purchase, barter, sale, storage, transportation, insurance or supply, or

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[7] Combines Investigation Act, 13-14 Geo. 5, c. 9; S.C. 1923. This Act repealed the Board of Commerce Act and Combines and Fair Prices Act.

[8] Ibid., s. 2 and s. 32. See: J.M. Magwood., Competition Law of Canada, Toronto: Carswell, 1981, at pp. 71-98 for an excellent review of the intervening amendments to 1960, none of which were more than rearrangements of the 1923 version. No jurisprudence developed during this period respecting mergers specifically.

> VI otherwise restraining or injuring trade or commerce, are described by the word "combine".

By section 32 of the Act: Everyone is guilty of an indictable offence and liable to a penalty not exceeding $10,000, or to two years imprisonment, or if a corporation to a penalty not exceeding $25,000, who is a party to or privy to or knowingly assists in the formation or operation of a combine within the meaning of this Act.

The first restatement of the merger provisions to be subject to critical judicial scrutiny, in the twin cases of Canadian Breweries and B.C. Sugar,[9] was the 1952 Combines Investigation Act[10] which had incorporated the MacQuarrie Committee's recommendations. Paragraph 2(a)(vi) defined a combine to include:

> "(vi) otherwise restraining or injuring trade or commerce, or a merger, trust or monopoly, which combination, merger, trust or monopoly has operated or is likely to operate to the detriment or against the interest of the public, whether consumers, producers or others."[11]

A merger, trust or monopoly was further defined in section 2(e) to mean one or more persons:

> (i) who has or have purchased, leased or otherwise acquired any control over or interest in the whole or part of the business of another, or
> (ii) who either substantially or completely control, throughout any particular area or district in Canada or throughout Canada the class or species of business in

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[9] See: Chapter II, section D, supra, for references to these two cases, from the "Group of Three".

[10] Combines Investigation Act, R.S.C. 1952, c. 314, as am.

[11] Ibid., par. 2(a)(vi).

which he is or they are engaged.'[12]

The charging provision was set forth in subsection 32(1) of the Act.[13] It becomes patently obvious that the intermingling of the merger provisions (s.2(e)(i)) and the monopoly proscriptions (s.2(e)(ii)) was a substantial source of confusion for the courts and counsel alike.[14] The 1960 amendments to the Act separated the two offences of illegal merger and monopoly; this subsequent revision remained the "law" until the current 1986 amendments. In simplified form, the 1960 provisions required that the Crown prove beyond a reasonable doubt three principal elements:

(1) A person "acquired" control over or interest in another person,

(2) Whereby competition was lessened,

(3) To the detriment of the public.

The first element was adopted from the 1952 amendments; the second and third find their origin in the Acts of 1923 and 1919 respectively. The 1960 Act was amended in 1976 to incorporate minor unrelated changes exhorted in the "Stage I" Amendments. While section 33[15] of the Combines Investigation Act, 1976, prohibited mergers, section 2 of the Act was the operative section defining the merger itself:

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[12] Ibid., subsection 2(e).
[13] Ibid., subsection 32(1).
[14] Both the B.C. Sugar and Canadian Breweries cases held that a merger had to lessen competition unduly, unduly being defined having regard to the structural market share test applied to monopoly offences.
[15] Combines Investigation Act, S.C. 1976, c. 76, s. 33.

> "merger" means the acquisition by one or more persons, whether by purchase or lease of shares or assets or otherwise, or any control over or interest in the whole or part of the business of a competitor, supplier, customer or any other person, whereby competition
> (a) in a trade, industry or profession,
> (b) among the sources of supply of a trade, industry or profession,
> (c) among the outlets for sales of a trade, industry or profession, or
> (d) otherwise than in paragraphs (a), (b) and (c),
> is or is likely to be lessened to the detriment or against the interest of the public, whether consumers, producers or others;[16]

Although the test for judging mergers has been subject to numerous proposed changes since 1960, the actual definition of a merger per se has remained unaltered until the 1986 amendments.

3. THE TEST FOR ILLEGALITY

(a) The Combines Investigation Act, 1976

The criteria upon which to judge the acceptability of a merger or proposed merger have progressed through numerous variations since the original Act of 1889,[17] the changes being symptomatic of the changes in contemporary policy objectives. For the past decade and a half the substantive provisions circumscribing mergers have been embodied in sections 2 and 33 of the 1976 Act.[18] Although no case law exists to confirm this assertion, it would appear that the 1976 test applied to horizontal, vertical and conglomerate mergers.[19] The test itself was a bifurcated approach covering both the structure of the market and the corresponding industry performance. The changes to the structure of the relevant market were monitored by examining whether "competition is or is likely to be lessened".[20] By subordinating the relevance of concentration and market share data, it may be argued with some merit that this standard was in fact a behavioural test.[21] This debate notwithstanding, the second requisite for an illegal merger necessitated a finding that the lessening of competition was "to the detriment or against the interest of the public, whether consumers, producers or others."[22] This is indisputably a performance criterion. The test as a whole was an indictable criminal offence,[23] to be tried pursuant to the procedure for indictable offences prescribed under the Criminal Code.[24] Consequently, some element of mens rea was required to be established by the Crown under a burden of proof beyond a reasonable doubt.[25] No guidance was supplied in the legislation to assist the courts in determining whether competition had been lessened or whether efficiency gains negated any anticompetitive repercussions. Arguably, the "public detriment" component of the section incorporated into the process the efficiency defence.

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[16] Ibid., s. 2.

[17] See: Magwood, supra, n. 8, at p. 41-98 for a review of the early provisions through to the 1960 amendments.

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[18] Originally amended in the Act of 1960; the most recent version is found in the 1976 Act, to which all further reference will be made. See: footnote 15, supra, for the citation and body of the section.

[19] Supra, n. 15, s. 2: The definition of a merger includes the acqisition of the business of a competitor (horizontal), supplier or customer (vertical), or any other person (conglomerate).

[20] Ibid.

[21] See: J.P. Cairns, "Monopoly, Detriment to the Public and the K.C. Irving Case", (1981) 30 University of New Brunswick L.J. 167.

[22] Supra, n. 15, s. 2.

[23] Ibid.

The leading, and only, judicial pronouncement which considered the merger provisions of the Combines Investigation Act, 1976, is the judgment of Laskin C.J.C., of the Supreme Court of Canada, in the K.C. Irving[26] case. Prior to the decision in K.C. Irving,[27] the courts had commingled the provisions respecting monopoly with the specific elements of the offence restricting certain mergers.[28]

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[24] See: sections 2 and 44(1) Combines Investigation Act, 1976, cited at n. 14, supra.

[25] A lingering issue, which was never resolved by the courts, questioned whether the requisite intent was to form the merger, lessen competition, or cause public detriment.

[26] K.C. Irving Ltd., [1978] 1 S.C.R. 408, 32 C.C.C. (2d) 1, 29 C.P.R. (2d) 83, 72 D.L.R. (3d) 82, 15 N.B.R. (2d) 450 (S.C.C.).

[27] See: Appendix B for a review of the essential findings of the major Canadian cases from the viewpoint of presumptive anticompetitive effects. The list is not restricted to "merger" cases because the early decisions did not clearly differentiate between the three major competition offences of conspiracy, monopoly and merger.

(b) Presumptions

The following perspective on recent Canadian jurisprudence endeavours to reduce the issues surrounding the two elements in the 1976 Act to one single query: What is the type of presumption which operated to assist the court in deducing the presumed fact from the basic fact. In this case, two causal relationships need to be examined: first, the link between increased concentration and the lessening of competition and secondly, the effect of this decrease in competition on the public interest. The form of presumption which operated may have been determinative in establishing a contravention of the merger provisions.

Presumptions have been divided into broad categories, presumptions of fact and presumptions of law. As Sopinka and Lederman summarize:

> Presumptions of law are a consequence "annexed by law to particular facts". A presumption of fact is "an inference which the mind naturally and logically draws from given facts, irrespective of their legal effect". Presumptions of law are either conclusive and irrebuttable, or rebuttable. Presumptions of fact are

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[28] In particular, see: R. v. Canadian Breweries Ltd. (1960), 34 C.P.R. 179, 126 C.C.C. 133, [1960] O.R. 601 (Ont.H.C.J.); R. v. British Columbia Sugar Refining Co. Ltd. and B.C. Sugar Refinery Ltd. (1960), 38 C.P.R. 177, 129 C.C.C. 7, 32 W.W.R. 577 (Man.C.A.); R. v. Morrey et al. (1956), 26 C.P.R. 55, 115 C.C.C. 337, 6 D.L.R. (2d) 405; 26 C.P.R. 55; 24 C.R. 319, 19 W.W.R. 299 (B.C.C.A.).

always rebuttable.[29]

The issue in the merger cases has been focused on the legal presumption, not the evidentiary presumption. A presumption relates only to the probative worth of the basic fact, not the presumed fact. In the example enunciated above between concentration and competition, a presumption is only probative of the basic fact that concentration has increased; the induction that competition has diminished is "presumed" only on the operation of a legal presumption. The presumption is not probative of the resultant state of competition. Consequently, the theoretical underpinnings justifying the application of the presumption are crucial.

A. T. Denning,[30] in a perspicacious article characterizing presumptions and burdens, emphasizes that the division of presumptions into those of fact and those of law "is comparatively modern in English law and should be replaced by a division into provisional presumptions, compelling presumptions and conclusive presumptions."[31] It is submitted that only four conceptual possibilities exist:

(1) Legal burden,

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[29] See: J. Sopinka and S.N. Lederman, The Law of Evidence in Civil Cases, Toronto: Butterworth's, 1974, at p. 375 et seq. for a clear distinction between these two concepts. See also: J.H. Wigmore, Anglo-American System of Evidence in Trials at Common Law, Boston: Little, Brown & Co., 1940, at par. 2491 et seq..

[30] A.T. Denning, "Presumptions and Burdens", 61 Law Quarterly Rev. 379.

[31] Ibid., at p. 379.

(2) Inference,

(3) Rebuttable presumption, and

(4) Irrebuttable presumption.

The basic paradigm describing presumptions is set forth by Professor Schiff;[32] the presumed or target fact is induced or inferred to be probative as a result of the existence of the basic fact.

The first type of presumption, the "legal burden" is not a true presumption at all; it is tantamount to the non-existence of a presumption. Denning defines a legal burden in the following manner:

> When the law puts on a party the burden of proving a certain fact in issue as a condition of giving him judgment, that burden never shifts and must be discharged or he will fail. ... the law places the burden of proof on the person who puts forward the proposition. This is the legal burden of proving the fact in issue. The incidence of it does not depend on whether the averment is positive or negative, for that can be varied by a change of language. It depends on the rules of substantive law which in this regard are ultimately the expression of public policy.[33]

Once the proponent who is subject to a legal burden proves the basic fact, on a balance of probabilities, the process is terminated. The respondent has no recourse. Viewing the legal burden from an alternate vantagepoint, one may equate a legal burden to an evidentiary burden; the law does not intervene to presuppose, by the operation of inductive reasoning substantiated by policy analysis, the existence of an adscititious presumed fact.

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[32] S.A. Schiff, Evidence in the Litigation Process, Toronto: Carswell, 1978.

[33] Denning, *supra*, n. 30, at p. 379.

A provisional presumption, or what is more commonly referred to as an inference,[34] has been described by Denning as a discretionary presumption; the court may draw the inference unless it is rebutted, but it need not do so. If the scales of evidence are equally weighted, the plaintiff, or applicant, would lose:

> Those relevant facts or circumstances are often said to raise a "presumption" or make a "prima facie" case, and so they do in the sense that from them the fact in issue may be inferred, but not in the sense that it must be inferred unless the contrary is proved.[35]

Schiff subdivides the concept of an inference into two subcategories. The justifiable inference is defined in the following manner:

> (1) When the existence of the basic fact is established, the existence of the presumed fact may be inferred by the application of the rules of logic. This seems to mean that the segment of human experience with which the court is familiar convinces the court that when the basic fact exists there is a reasonable probability that the presumed fact also exists. In such a situation the courts speak in terms of justifiable inference or presumption of fact.[36]

The second version of an inference does not appear to be warranted.[37] With respect, an inference should be distinguishable from a "compelling presumption". In the former case, if the applicant's evidence is not rebutted the applicant does not necessarily succeed; in the latter case, unless the respondent successfully refutes the presumed fact, or balances the evidentiary scales, the applicant will succeed.

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[34] Synonyms for an "inference" are a suggestive, natural, permissive presumption or Praesumptiones hominis.
[35] Denning, supra, n. 30, at p. 380.
[36] Schiff, supra, n. 32, at p. 1136.
[37] Ibid.

Denning's "compelling presumption" has frequently been referred to as a prima facie test, a rebuttable presumption or a mandatory presumption.[38] The distinguishing ingredient of the rebuttable presumption is the requirement that the court shall draw the conclusion of the validity of the presumed fact unless the respondent rebuts. In practice, a rebuttable presumption places a much heavier burden on the respondent than does an inference. As Schiff defines the rebuttable presumption:

> When the basic fact is established, the existence of the presumed fact must be assumed unless and until certain specified conditions are fulfilled.[39]

It may be said that the rebuttable presumption creates a reverse onus. As Professor Schiff notes:

> [J]udges have consistently placed on the opponent of the compelled determination both the burden of introducing evidence and the burden of persuasion.[40]

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[38] Alternate terms found in the literature for a rebuttable presumption is an inconclusive, mandatory or "compelled - unless" presumption or a praesumptiones juris tantem.

[39] Schiff, supra, n. 32, at p. 1137.

[40] Ibid., at p. 1143.

If one analyses the possible reasons for applying a presumption of law, it becomes clear that a rebuttable presumption was not applicable to the previous merger provisions of the Combines Investigation Act. Of the following rationale which have been proposed for the employment of presumptions, public policy must stand as the only credible justification:

(1) To expedite trials,

(2) To avoid a procedural impasse,

(3) To overcome the impossibility of obtaining evidence,

(4) One of the parties is privy to particular knowledge or information, and

(5) Public policy justifies its use.

Unfortunately the economic justification for applying a rebuttable presumption to infer anticompetitive conduct from monopolization, or to infer public detriment from a diminution of competition, is tenuous at best. In the case of the Combines Investigation Act, the reverse onus was inconsistent with the Criminal law presumption of innocence. Even in the case of the civil burden instituted in the new Competition Act, the presumption would violate the legal maxim, he who alleges must prove.

The final form of presumption is the conclusive or irrebuttable presumption.[41] In circumstances subject to a conclusive presumption, the presumed fact is incontrovertibly inferred from the basic fact; the respondent has no opportunity to dispute the presumption. As Denning states:

> It is a misuse of language to speak of any presumption being conclusive, but the meaning is clear enough. On proof of certain facts the Court must draw a particular inference, whether true or not, and it cannot be rebutted.[42]

As Professor Schiff explains:

> When the basic fact is established, the existence of the presumed fact must, for the purpose in hand be permanently and unconditionally presumed. This obviously means that the basic fact is legally the equivalent of the presumed fact... [43]

(c) The Effect Of The K. C. Irving Case

Several well-respected students[44] of Canadian competition policy have endeavoured to interpret Chief Justice Laskin's judgment in the K.C. Irving case. The outcome of the analysis is necessary to understand the continuing interest in government and academic circles to revamp the merger laws. Most writers advised, as a consequence of the *K.C. Irving* decision, that the substantive test governing merger activity should be tightened and made more restrictive. Now that the Competition Act has finally been proclaimed, one must regard the "improvement" with some skepticism and uneasiness.

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[41] Also labelled an absolute presumption of praesumptiones juris et de jure.

[42] Denning, supra, n. 30, at p. 381.

[43] Schiff, supra, n. 32, at p. 1137.

[44] Most notable of the commentaries are: J.P. Cairns, "Merger Policy in Canada and the Supreme Court of Canada Decision in K.C. Irving, Ltd." (1981) 19 Alberta L.R. 303; J.P. Cairns, "Monopoly, Detriment to the Public and the K.C. Irving Case", (1981) 30 University of New Brunswick L. J. 167; G.B. Reschenthaler and W.T. Stanbury, "Benign Monopoly: Canadian Merger Policy and the K.C. Irving Case", (1977) 2 Can. Business L. J. 135.

In *K. C. Irving*, the Supreme Court of Canada was asked to decide whether the lower courts had erred in law on three major issues: the definition of competition, the meaning of detriment and the availability of legal presumptions. In essence, the Crown argued that the establishment of a virtual monopoly proved by way of rebuttable presumption that competition had been lessened unduly and therefore public detriment resulted. Pursuant to sections 2 and 33 of the Combines Investigation Act, 1976, Laskin categorically rejected the Crown's contentions. There was *no* requirement of "unduly"[43] nor was the element of "control" of the market[44] a prerequisite for conviction. In unadorned simplicity, no rebuttable presumption operated in the concentration - competition - detriment causation model. As Laskin, C.J.C. concluded in a frequently cited quotation:

In the light of the definition of "merger" in the

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[43] *Irving*, *supra*, n. 26, at p. 10 C.C.C.
[44] This is in contradistinction to "control" of the acquired firm.

> present Combines Investigation Act it is impossible to say that acquisition of entire control over a business in a market are (as contrasted with acquisition of some control) must mean without more not only that competition therein was or was likely to be lessened but that by reason of such control the lessening or likely lessening is to the detriment or against the interest of the public. Even if the acquisition of entire control would be enough to support an inference of lessening or likely lessening of competition, that inference cannot be drawn here, in the face of the evidence and the findings thereon by the trial Judge and by the Court of Appeal that the pre-existing competition where it existed, remained and was to some degree intensified by the take-over of the newspapers.[47]

As Professor Cairns argued, the phrase "without more" seemed to imply a "double-barrelled" test. An illegal merger was one that both decreased competition and operated to the detriment of the public independent of the lessening of competition.

This possible interpretation of the K.C. Irving judgment would require a separate determination that the merger was detrimental to the public. An extremely preplexing issue underlies the accepted economic wisdom. It is generally assumed that "the more rivalry the better". Conversely, a decrease in rivalry must be detrimental to the public. However, if one considers there to be an "optimal" level of competition, it is conceivable that a decrease in rivalry may be preferred. To initiate an examination of this hypothesis, it is recommended that future study investigate the meaning and measurement of "rivalry". As a result of anlayzing the policy reasons for the 1960 amendments, Professor Cairns rejected the "double barrel" interpretation:

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[47] K.C. Irving, at p. 12-13.

> If this interpretation of the judgment is correct, both offences require proof of operation detrimental to the public. It is difficult to believe that the 1960 amendment which clearly differentiated between the two offences was intended to have this result.[48]

Cairns preferred a "single barrel" test; any lessening of competition was presumed to be detrimental to the public. This approach would more closely parallel the American provisions in section 7 Clayton Act. It is extremely interesting to note that if Professor Cairns' interpretation of the "single-barrelled" approach were correct, the test would reduce to requiring no proof of detriment, only a lessening of competition. When viewed in this light, the new provisions under the Competition Act, which require proof of a substantial lessening of competition, are more restrictive on the Crown. This does not appear to be compatible with Mr. Cote's stated intentions.

The third interpretation of Chief Justice Laskin's obiter would require proof that detriment "flowed from" the lessening of competition. It is respectfully submitted that this third interpretation is the correct one to be applied to the former merger proscriptions in the Combines Investigation Act. The Crown was obliged to prove both elements of the criminal offence: the lessening of competition and the detriment to the public which flowed from the lessening of competition. On first blush, it would appear that the Crown would be subject to a lesser evidentiary burden under the new provisions. However, it is submitted that this hope may not be fulfilled. First, the Crown must still prove that the lessening of competition was "substantial". This may be judicially interpreted to be analogous to the "public detriment" element in the former Act. Secondly, if competition is defined to mean "rivalry" in the Cairns' context,[49] then under the former Act the Crown would have been required to prove only a lessening of competition, whereas under the Competition Act the diminution must be substantial. As well, the efficiency defence, the s.64(2) "concentration-plus" requirement, and the s.65 "factors to be considered" will inevitably be reduced to an analysis of the current economic conditions, an examination which will be not unlike the evaluation of "public detriment". It is not at all certain that the substantive test itself under the Competition Act is preferable to the former standard. The shift to the civil burden of proof is universally accepted as an improvement;

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[48] Cairns, supra, n. 44, "Merger Policy in Canada", at p. 320.

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[49] Cairns, supra, n. 44, "Monopoly, Detriment to the Public, and the K.C. Irving Case", at p. 185.

the new test for reviewability may not be.

3. REMEDIES

A detailed summary of the chronological development of the proposals for remedial relief since the Skeoch-McDonald Report may be found in Appendix A. It is the intent of this section to highlight the changes to the former Combines Investigation Act which are found in the present Act. The new injunction provisions will be discussed at length in Chapter VII infra. Because the substantive provisions in the new Act are categorized as "reviewable trade practices", the concept of fines and imprisonment for contravention of an "offence" are not appropriate and have therefore been omitted. Conditional orders[30] have been made available to vary an original s. 64 dissolution order in cases where customs duties, regulations on imports or any action specified in the order will present the merger from lessening competition substantially. One must question the rationale for restricting government imposed entry barriers to international trade factors. The former section of the Combines Investigation Act which granted Cabinet the jurisdiction to reduce tariffs which protected uncompetitive markets[31] has been retained but modified to reflect the new substantive test. Of note is the retention of the civil damages provisions in section 31.1 of the former Act; however, this remedy will not be available to recover damages resulting from an offensive merger unless an order, granted by the Tribunal or the court, has been ignored.

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[30] Competition Act, s. 71.

[31] Ibid., s. 28.

The remedies available to the Tribunal are available in the case of a completed merger[52] as well as in the case of a proposed merger.[53] For each type of merger, either completed or proposed, the form of remedy may be characterized as either mandatory or prohibitive.

Turning first to completed mergers, the Tribunal may, at its discretion, unilaterally order any party to dissolve the merger or dispose of assets. In addition to or in place of a dissolution or divestiture order, the Tribunal may, with the consent of the party and the Director, grant a consent order.

These consent orders may be in the form of either an order of prohibition or an order of mandamus. Notice for completed mergers that both forms of order require consent. This ability conforms with the objectives of the Department to foster voluntary compliance and to encourage the parties to enter into undertakings.[54] In addition, because these orders involve direct participation in the operations of the company, consent is required.

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[52] Ibid., s. 64(1)(e).
[53] Ibid., s. 64(1)(f).
[54] See: Chapter IX on conglomerate mergers and the review of the Imasco/Genstar undertakings.

With respect to proposed mergers, the Tribunal "may make an order directed against" any party to the merger not to proceed with the merger or part of the merger.[55] It is envisioned that this order could take the form of a "cease and desist" order prohibiting any action in furtherance of the merger. Or, the order could require divestiture of certain assets or holdings before the merger could proceed. The latter would allow the parties to proceed with the merger, but it would impose a condition precedent. In addition to, or in lieu of these orders, the Tribunal may impose a prohibition order on any party without consent.[56] The prohibition order would allow the merger to proceed subject to certain conditions imposed on the transaction by the Tribunal. These conditions would ensure that competition would not be lessened substantially. In a K.C. Irving situation, a prohibition order of this nature could require that the editorial boards be kept separate. In the case of a mandatory order directing the corporation to do certain acts, the consent of the parties and the Director is required. As above, consent of the parties is necessary because the order requires direct involvement in the operation of the company, as well as because the object is to foster voluntary compliance.[57]

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[55] Competition Act, s. 64(1)(f)(i), (ii).

[56] Ibid., s. 64(1)(f)(iii)(A).

The relief provisions under the Competition Act provide a wide variety and tremendous flexibility to accomodate mergers while protecting the public interest in competitive markets. The order of the Tribunal may even apply to any person outside the transaction.[58]

B THE SUBSTANTIVE MERGER TEST UNDER THE NEW ACT

1. INTRODUCTION

As has been mentioned early in this paper, the advantage of shifting to civil procedure, with its less onerous burden of proof, cannot be underestimated. The merger provisions in the new Act are now designated as a reviewable trade practice. All mergers, therefore, are lawful, unless successfully challenged by the Director. This methodology is more permissive than the American system which prohibits outright mergers which substantially lessen competition or tend to create a monopoly.

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[57] Ibid., s. 64(1)(f)(iii)(B). This view is attributed to Professor R. Nozick, Faculty of Law, University of Alberta.

[58] This provision is necessary so that the order would be capable for example of freezing the shares of Fathom in National Victoria and Grey Trust Company. See: A.G. Canada v. Fleet Aerospace et al.; unreported, March 27, 1985, Federal Court Trial Division, T-494-85.

The new provisions will be reviewed below by dividing the discussion into three major headings: the definition of a merger, the actual test and the exemptions to an otherwise reviewable merger. Finally, an effort will be made to predict the probable effectiveness of the new provisions.

2. THE DEFINITION OF MERGER

Section 63 establishes the definition of a merger as follows:

> 63. In sections 64 to 72, "merger" means the acquisition or establishment, direct or indirect, by one or more persons, whether by purchase or lease of shares or assets, by amalgamation or by combination or otherwise, of control over or significant interest in the whole or a part of the business of a competitor, supplier, customer, or other person.[11]

The definition may be disected into five constituent elements. First and foremost, the merger must be an "acquisition or establishment, direct or indirect". Certain express examples are given of an aquisition but the Act does not define this term. It is submitted that the courts may be required to interpret this aspect of the definition due to the inclusion of "or otherwise" in the section. Furthermore, the establishment of control over a business "indirectly" may contemplate the acquisition by a holding company of another holding company. The acquired firm may control a company several times removed down the corporate chain. The acquiring firm and this distant "subsidiary" may be in competition. Presumably the "50% Rule" would apply to define the acquiring firm and the distant subsidiary of the acquired firm as a "merger". As well, the definition recognizes that two or more firms could enter into a joint venture agreement to acquire a third party.

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[11] Competition Act, s. 63.

The second element of the definition enumerates five types of acquisitions:

(a) purchase or lease of assets,

(b) purchase or lease of shares,

(c) amalgamation,

(d) combination, or

(e) otherwise.

Several crucial points must be made regarding this list. First, the definition of "merger" as an "acquisition" must not be confused with the type of "transaction" which triggers the requirements under the pre-notification provisions. Section 64 applies to mergers; section 86 applies to transactions. The definition of merger is broader in scope because of its inclusion of other forms of acquisitions. Second, a merger could conceivably include such business relationships as partnerships, consortiums and cartels. Third, the choice of the term "combination" might resurrect the antiquated "combine" and with it the jurisprudence which relied heavily on monopolization concepts and notions of "unduly".

"Control over or significant interest in" a business is the third prerequisite in the definition. As a consequence of the view expressed in past commentaries, care must be taken not to confuse control over a business with control over the market. There is no definition of "control" nor for "significant interest" supplied in this section. In Bill form, this section implied "voting" control or "effective" control. This was presumed because the legislators desired to require de facto[60] control, and because the "50% Rule"[61] defining "control" applied under the pre-notification provisions was omitted. It would have been difficult to argue that this omission was merely an oversight. Because the Department felt that de facto control was too vague for the business community, the "50% Rule" now defines "control" within the merger definition of the Act. This is definitely a shortcoming of the definition; with the complex share holdings of contemporary supercorporations, a minority shareholder position may often yield effective control. Besides this definition now casts doubt over the meaning to be attributed to the phrase "significant interest". May the control of shares be something less than fifty percent? May the control of assets be less than the fifty percent control required for shares, thus being transaction non-neutral? May the control of a business be accomplished by establishing interlocking directorships?

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[60] See: House of Commons. Minutes of the Legislative Committee on Bill C-91, Second Reading, at p. 8:15; See also testimony of ADD Capp, at p. 10:25.

[61] Bill C-91, s. 38.

Although section 2(4) states that the "50% Rule" applies to the entire Act, it is submitted that the more reasonable interpretation of "control" in the definition of merger implies de facto control. It would be unreasonable to require pre-notification when twenty percent of shares had been acquired, then define a merger only when the fifty percent threshold has been exceeded. Furthermore, the concept of "significant interest" would imply de facto control. Unfortunately, the meaning of "control" in the definition of a merger is far from settled.

The fourth element in the definition is the requirement that the "whole or a part of a business" be controlled. This is not the same as the "operating business" requirement in s. 80 which governs notifiable transactions. The policy implications of this distinction are unclear. Presumably both sections are ultimately concerned with businesses which lessen competition substantially.

The type of business that must be acquired completes the definition. It would appear that the acquisition of any other business would satisfy the section; consequently the need to specify "competitor, supplier, customer" seems redundant. Only if the concept of competition is restricted by the Tribunal to the horizontal effects of mergers, would the phrase be relevant. Even in this case, conglomerate mergers could exhibit horizontal effects on competition through reciprocity. It is submitted that the emphasis in the current definition to horizontal and vertical mergers results from the adoption of the phraseology employed in section 2 of the former Combines Investigation Act. All three forms of mergers may be reviewed under the new Act.

When compared to the former definition of merger, the present standard places a greater evidentiary burden on the Director. The former Act only required proof of "any [emphasis added] control over or interest in" another's business; whereas the present definition necessitates establishing "control ["50% Rule"] or significant [emphasis added] interest" in the business of another. This heavier burden of proof will tend to neutralize any "alleged" advantage the Director may have had under the substantive test enacted in section 64.

3. THE STANDARD FOR JUDGING MERGERS

On first blush, the substantive test appears to be quite straightforward. The Director must convince the Tribunal that the "merger or proposed merger prevents or lessens, or is likely to prevent or lessen, competition substantially"[63] in the relevant market. The determination of a substantial lessening of competition shall not be based

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[63] Competition Act, s. 64(1).

"solely on the basis of evidence of concentration or market share."[63] The Act supplies a "laundry list"[64] of factors which may be considered by the Tribunal in its determination. The efficiencies defence[65] has been retained. If the Tribunal finds on review that the merger has satisfied the conditions of section 64, specified mandatory, prohibitive and permissive orders are available to rectify the anticompetitive impact of the merger.[66] Note that the requirement of intent has not been included.[67]

The ever present problem of delineating the relevant market will be crucial to the operation of this standard.[68] The phraseology "is likely to prevent" has never been accorded the importance that it should. It is submitted that this phrase encompasses the conglomerate merger scenario and its impact on aggregate concentration. A shortcoming of all the previous proposals, and one from which the present provisions are not immune, is the reliance on "tombstone information". The reliability of past data to predict the effect on future competition levels is subject to all the same limitations which restrict the usefulness of

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[63] Ibid., s. 64(2).
[64] Ibid., s. 65.
[65] Ibid., s. 68.
[66] Ibid., s. 65(e),(f). See: Chapter V A-4 for a review of the remedies under the new Act.
[67] See: Bill C-29, s. 31.74(1)(g).
[68] See: Chapter IX, for a detailed discussion of this problem.

"playometrics".

It is not certain that the new test will be any more advantageous to the Director than the former section under the Combines Investigation Act.[‘’] Although Chief Justice Laskin's comments on the presumption of detriment in K.C. Irving were only dicta, it is probable that proof of detriment would have been required under the former Act. The practical effect of the new Act requiring a "substantial" lessening of competition rather than a "detrimental" lessening of competition may prove to be a distinction without a difference. On the other hand, if the former provisions never did require proof of detriment, the "improvements" may be a retreat.

On Second Reading of Bill C-91, concern was raised by several members of the Legislative Committee over the treatment of mergers involving a foreign acquiring firm. The issue raised was whether clearance under the Investment Canada Act would preempt review under the Competition Act. It is the view of the Department of Justice that all mergers "in Canada" would be subject to the provisions of the Act. Mr. M. Rosenberg of the Department of Justice, stated:

> I am sorry, I do not have the Investment Canada Act here, but section 34 of the Investment Canada Act quite clearly states something to the effect that nothing in

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[‘’] See: Chapter V A-3(c) for a more detailed review of these two issues.

> the Investment Canada Act affects the operation of any other act of Parliament with respect to an acquisition that is the subject of the Investment Canada Act.[70]

Mr. M. Capp, Assistant Deputy Director of the Department of Consumer and Corporate Affairs, confirmed this view:

> Mr. Chairman, may I just point out, as Mr. Rosenberg indicated, the Investment Canada Act is merely saying that you are permitted to enter the country; it does not say you are unequivocally approved to break the laws of the land. Just as those companies have to live within the corporations law and securities law, they would have to live within the Competition Act as well.[71]

The reasoning for the inclusion of subsection 64(2) (Evidence) is puzzling. The subsection states:

> (2) For the purpose of this section, the Tribunal shall not find that a merger or proposed merger prevents or lessens, or is likely to prevent or lessen, competition substantially solely on the basis of evidence of concentration or market share.[72]

The Tribunal "shall" not determine the anticompetitive effect of a merger "solely" on evidence of concentration or market share. In the case of a virtual monopoly, it would appear that the operation of a rebuttable presumption, even one which is judicially developed, is expressly excluded. This condition is consistent with the rationale in K.C. Irving but may place a demanding burden of proof on the Director. Conversely, if the theory which proposes that concentration has no effect on industry performance in adopted, then this subsection may be misleading. Does this subsection require, as a necessary condition to satisfy s. 64(1), that concentration or market share has been increased? If this view is adopted by the Tribunal, then a doctrine of "concentration plus" may evolve. The Director would be required to prove, as a necessary condition, that concentration or market share had increased as a result of the merger plus something more. These supplemental circumstances may take the form of a natural predilection to collusion, price leadership or effective barriers to entry. In essence, in order to prove a substantial lessening of competition, the Director must establish an increase in concentration or market share plus any other S.65 factor relevant to determining the effect on competition.

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[70] House of Commons, Legislative Committee Hearing Bill C-91, Second Reading, at p. 11:44-45.

[71] Ibid., at p. 11:45.

[72] Competition Act, s. 64(2).

The frightening aspect of S.64(2) is its reliance on concentration measures at all. It is trite to repeat at this stage that a decrease in concentration may also decrease competition in a market. As a consequence, the Tribunal will have no alternative but to evaluate the merger effects on the basis of the "laundry list" of factors enumerated in section 65. At this point the analysis will deteriorate into a process not unlike the evaluation of the concept of detriment. It would appear that this subsection is the result of attempts to compromise between one economic stream of thought which subordinates the importance of concentration as only one characteristic of industry structure,[73] and another which argues that the ability to collude is correlated with concentration.

A final note regarding the substantive test for mergers. If Parliament intended to downplay the role of concentration in measuring competition, then some effort should be directed towards defining and measuring this term. This will not be an easy task. As the Act now stands the allocative and distributional judgments of an expert Tribunal are being substituted for decisions determined by the unbiased price mechanism of the free market. As Steven Globerman concluded:

> The recent Amendments to the Combines Act do not, therefore, represent a substantial step forward toward promoting free and fair competition. Rather, they continue a tradition of substituting the judgment of government appointed "experts" for the judgment of the marketplace. Whether Canadians would be better off without the merger amendments or, indeed, without the entire Combines Act, is at least a debatable question.[74]

The factors to be considered in determining a prevention or lessening of competition embody the heart of the new test. Except for the "effective competition remaining" (s. 65(e)) and the "other factors" (s. 65(h)) subsections, it appears that the general objective of the list is to define the structure of the industry.[75] The factors which appeared in Bill C-29 but which have been omitted from the new Act exhibit a greater affinity for conduct criteria than do the present factors. Section 31.74(1) Bill C-29 had included in addition to those factors presently contained in the Competition Act:

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[73] See: Skeoch-McDonald Report, at p. 86.

[74] Steven Globerman, "The Merger Provisions of Bill C-91: An Evaluation", in Reaction: The Combines Investigation Act, Vancouver: The Fraser Institute, 1986, at p. 112.)R

(a) The history of anticompetitive conduct,

(b) The foreclosure of sources of inputs and outlets,

(c) The likelihood the merger would stimulate competition, and

(d) The size differentials of the merging partners and their competitors.

The Honourable Michel Cote, in his testimony before the Legislative Committee, explained that these factors were excluded because they were either repetitive or they could be incorporated into the Act by way of the "basket clause" (s. 65(h)).[76]

Foreign competition (s. 65(a)), acceptable substitutes (s. 65(c)), barriers to entry (s. 65(d)) and technological change (s. 65(g)) are all factors which assist in defining the relevant market. The failing company defence, along with the efficiencies defence are the two defences provided in the 1982 American Merger Guidelines. And removal of a vigorous competitor (s. 65(f)) is a factor which may facilitate collusion in the industry. These factors are all included in the American Guidelines; the one aberration in section 65 is the "effective competition remaining" test. It is suggested that this factor has been included as a result of intense lobbying by the business community and also simply as a result of a carry-over from Bill C-29.[77] This factor may resurrect the arguments accepted in the B.C. Sugar and Canadian Breweries cases; these judgments established a "quasi-defence" for the defendants if they were able to establish that effective competition remained in the market. It is submitted that this factor greatly diminishes the effectiveness of the substantive test from the Director's perspective.

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[75] See: Skeoch-McDonald Report, supra, n. 73. Note that two additional factors were added to Bill C-91 before proclamation: removal of a vigorous competitor and the nature of technological change, both acceptable to the authors of the Report.

[76] Legislative Committee Hearings, supra, n. 69, at p. 1:30.

The approach employed in the new Act to determine the market power resulting from a merger is an ex post market share process. The market share and concentration levels are estimated then interpreted subject to the S.65 factors. This method is in direct contrast to the DOJ Merger Guidelines developed in the United States. Two comments are offered. First, the Director will still be compelled to at least approximate the market share in order to subsequently adjust it. Secondly, an ex post modification process runs a high risk of neglecting fundamentally vital factors. As evidenced by the new provisions, noticeably absent are supply substitution, geographic substitution and the concept of potential competition.

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[77] Bill C-29, s. 31.74(1)(k).

4. EXEMPTIONS

(a) Specific Exemptions

Subsection 64(a) requires the Tribunal to exempt any merger "substantially completed" before the section is proclaimed. It is highly unlikely that this section created any inducement to merge prior to the coming into force of the Act due to the uncertainty surrounding its passage through the House. This is particularly true in light of the government's former track record in proposing reform. This transitional provision is desirable.

Subsection 66(b) exempting acquisitions or amalgamations under the Bank Act is less tenable. It has always been impliedly presumed in the economic literature that competition policy did not apply to regulated industries. If this precept had been applied in the Act there would not be the need to expressly exempt the highly regulated banking industry. Regulated industries have been exempt from the operation of the former Combines Investigation Act if the activity in question was empowered by the legislation.[78] In the case of mergers involving firms in a regulated industry, unless the enabling statute expressly empowered the firms to merge, the Combines Investigation Act would apply. If the cases under the old Act are applied to the Competition Act, mergers in regulated industries will be subject to its provisions. Given the federal government's moves in recent years to deregulate the banking industry, the preferential treatment afforded the financial sector and not the transportation, communication, public utility and other regulated sectors is unwarranted. A logical inference to be drawn from section 66(b) is that the only regulated industry to be sheltered from the policy underlying the Competition Act is the banking industry.

(b) Joint Ventures

A combination is not defined in the Act but would logically apply to all mergers which were neither acquisitions nor amalgamations. Two forms of combinations possibly envisaged by the policy makers could be partnerships and joint ventures. The concept of a combination is primarily a construct to permit the exemption of certain joint ventures.

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[78] For a discussion of the Regulatory Exemption, see: R. Nozick, "Anticompetitive Agreements Under the Combines Investigation Act", (1985) 14 Man.L.J. 379. Note also: s.80(2) Competition Act intends to catch mergers between Crown corporations.

A joint venture is also not defined in the Act; the pre-notification provisions imply that a joint venture is a combination in which all parties contribute assets, do not change control and specify a termination date for the project.[79] These "joint ventures" are exempt from the notification and inform provisions under section 86. A second and smaller set of "joint ventures" is exempt from the substantive test if, in addition to the above three characteristics, they undertake a specific project or program of R & D and

(a) the project or program would not have proceeded "but for" the joint venture, and

(b) the project or program minimizes the anticompetitive effect, or strives for "minimum detriment".[80]

Consequently, not all joint ventures are excluded from review under section 64. Yet all joint ventures are excluded from pre-notifying. This is a complete reversal from the reasonable approach of requiring all joint ventures to notify, then exempting certain sectors "targeted" for preferential treatment.

Concern has been raised that incorporated joint ventures should also be accorded this exemption. The Canadian Bar Association's "Submission on Bill C-91" urged that:

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[79] Ibid., s. 84.
[80] Ibid., s. 67.

> [W]e see no reason why the exception in section 67 should be restricted to unincorporated joint ventures. There may be valid significant reasons, for tax or other purposes, for conducting a joint venture through the vehicle of a corporation and we do not see the justification for excluding this flexibility. It appears to us that a jiont venture in corporate form can be subjected to all the constraints set forth in section 67 and can be monitored just as adequately as an unincorporated joint venture.[81]

As mentioned infra under pre-notification, this may have permitted firms to circumvent the legislation for pre-notification. But with respect to the substantive provisions, only projects or programs in R & D satisfying the "but for" test and the "minimal detriment" criterion could have been sheltered under this "incorporation umbrella".

(c) Efficiencies

The efficiencies defence is set forth in section 68(1) as:

> 68.(1) The Tribunal shall not make an order under section 64 if it finds that the merger or proposed merger in respect of which the application is made has brought about or is likely to bring about gains in efficiency that will be greater than, and will offset, the effects of any prevention or lessening of competition that will result or is likely to result from the merger or proposed merger and that the gains in efficiency would not likely be attained if the order were made.[82]

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[81] Canadian Bar Association, "Submission on Bill C-91", Special Committee on the Combines Investigation Act, May, 1986, at p. 18.

[82] Competition Act, s. 68(1).

It is a two-pronged test requiring the balancing of efficiencies to the parties and the effects on competition to the community plus the establishment that the gains in efficiency would not be attained "but for" the merger.[83] The onus is on the defendant.[84] The inherent problem with this test is that the gains in efficiency and the effects of market power are incommensurable. Furthermore, there is an everpresent danger that the efficiency gains will be more identifiable than the effects of the more illusory concept of market power.

It is perplexing why export and import competition have been given a prominant role in determining gains in efficiency.[85] Why should efficiency gains on goods for export be given priority over efficiency gains for domestic goods?

Finally, subsection 68(3) is certainly justified on economic grounds; the legislators are emphasizing their concern over deadweight social loss. It is highly unlikely that the non-economist members of the Tribunal will be comfortable with this doctrine.

(d) Limitations

Section 69 limits an application under section 64 to three years after the merger has been substantially completed. Although the Canadian Bar Association recommended one year, the present position seems preferable.

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[83] See: supra, n. 70, at p. 11:42.
[84] Ibid., at p. 11:41.
[85] Ibid., s. 68(2).

(e) Multiplicity

Section 70 precludes an application under the merger provisions if there is also an application brought under the conspiracy[66] or abuse of dominant position[67] provisions. The objective of this provision is to minimize harassment by the Director. The disadvantage as explained by former Director Lawson Hunter is, "it is true it forces him [the Director] to an election."[68] Before proceeding, the Director must choose between which of the provisions is most appropriate.

5. CONCLUSIONS

The underlying objective of reforming merger policy has been to afford the Director a greater opportunity to restrict the behaviour of large anticompetitive mergers. To this end, the proponents of the new legislation argue that the lower burden of proof and the elimination of the "public detriment" element have accomplished this goal.

The skeptics point to the heavier burden of defining a merger. As well, the concept of "rivalry" and the "shopping basket" of available defences, primarily the "efficiencies" and "effective competition remaining" inclusions, do not auger well for real reform.

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[66] Competition Act, s. 32.
[67] Competition Act, s. 51.
[68] Supra, n. 70, at p. 8:8.

With regard to guidelines for injunctive relief, the salient features of the test must be retained while the defences discarded. The argument in favour of such a recommendation is offered in chapter IX infra.

In sum, the functionality of the provisional injunction provisions[''] will depend almost completely on the interpretation given to the substantive provisions. If the test emerges ineffectual, so also the provisional relief provisions.

[''] Competition Act, s. 72, 76.

VI PRE-MERGER REQUIREMENTS

A THREE TYPES OF PRE-MERGER REQUIREMENTS

The requirement to notify the Director of Investigation and Research before the legal consummation of the merger has long been urged by experts in the field of competition policy. The different mutations on pre-merger reporting requirements may be compiled into three broad categories:

1. Registration requirements;
2. Pre-clearance requirements, and
3. Pre-notification requirements.

Each of these classifications may be further subdivided into mandatory and permissive obligations. The registration requirements simply necessitate the registration of all mergers with the appropriate government agency. The registration scheme may require registration of pre-merger proposed transactions or post-merger completed acquisitions. However, registration procedures have connoted ex post facto notification. A size threshold can be included to eliminate economically insignificant combinations. A final issue that must be resolved is whether or not the reporting requirement is to be mandatory or permissive. If it is designed to be permissive, the question must be addressed as to what ramifications will flow from voluntary avoidance of the provisions?

Pre-clearance provisions, often referred to as advance ruling conditions, must be, by definition, voluntary on the part of the parties to the merger. If the advance ruling provisions were mandatory on the merging firms, then such stipulations would be viewed as what has come to be termed pre-notification provisions. It is trite and nonsensical to consider post-merger or cut-off thresholds for pre-clearance provisions.

The third variant of pre-merger reporting is the pre-notification requirement. Much emphasis has been placed on such a provision in recent years.

The distinguishing features of a pre-notification requirement are the following:

(a) Notification is required before the consummation of the merger;

(b) At least some mergers are required to notify;

(c) The notification must be accompanied by prescribed information;

(d) The Director is under an obligation, either directly or indirectly, to determine the acceptability of the merger.

The advance ruling procedures, although instituted before the consummation of the merger, are distinguishable in that they are neither mandatory nor do they require a decision to be made by the Director. The registration procedures may accept notification after the merger and have no jurisdiction to require relevant financial and economic information.

Several forceful arguments have been presented in favour of such a requirement. Firstly, the available remedies to dissolve or divest the parties after the merger result in tremendous misallocations of resources which might possibly outweigh the negative impact on competition and efficiency sought to be averted. Secondly, innocent third parties may be subject to damages. Finally, it is the fervent hope of the proponents of such propositions, that early analysis by the Director of Investigation and Research will foster certainty and predictability in the business community. The issue of whether or not to apply a transaction threshold concordant with the definition of a merger prescribed in the substantive sections of the Act is controversial. Again, the effect of structuring the scheme as a mandatory or voluntary requirement must be addressed. Moreover, an intriguing policy issue arises when one considers the effect of the adjudicative body remaining mute on the acceptability of the proposed merger. Does silence imply acceptance, rejection or indecision subject to future challenge?

B RECENT DEVELOPMENT OF THE PRE-MERGER REQUIREMENTS

1. THE ORIGINS OF NOTIFICATION

(a) Registration Provisions

The present Act does not contain any form of post-merger registration requirement. The former Combines

Investigation Act contained no reporting requirements whatsoever. The Economic Council, in their Interim Report, endorsed a registration procedure:

> A very important part of the procedure with regard to mergers would be a process of selection. It would be essential that this process ensure timely consideration of all mergers in which there was a significant potential for harm. Appropriate procedures should be initiated to accomplish this objective in a regular and comprehensive way. If necessary, a registration procedure could be implemented.[1]

Bill C-256 attempted to implement the Economic Council's recommendation by requiring all mergers whose assets or sales would be greater than five million dollars to be registered before or within two weeks after the merger.[2] The effect of such registration was to limit the Competitive Practices Tribunal's challenge to one year after registration.[3] Tangentially, it is interesting to note that all foreign mergers were required to register.[4] The criticism of such a pre-merger reporting scheme is twofold. First, the allowance of post-merger registration and challenges by the Commissioner after the consummation of the merger does little to mitigate the concern surrounding the additional "excess burden" of dissolving a consummated merger. Secondly, the ability of the tribunal to challenge the merger for one year subsequent to registration does not increase certainty and reliability in the business community.

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[1] Interim Report, p. 115

[2] Bill C-256, S.32(1)

[3] Ibid., S.32(4)

[4] Ibid., S.33

(b) Pre-Clearance Provisions

In conjunction with the registration procedure, Bill C-256 proposed an Advance Ruling provision[5] which would allow a party to the merger to apply to the Tribunal for a mandatory determination[6] of whether or not the merger would be subject to an order under the substantive test of unlawfulness.[7] The Commissioner (Director) was also given discretionary authority to request a predetermination of the issue by the tribunal under the identical section. The Tribunal would have the discretion, at this juncture, to pre-clear any modifications agreed to by the parties that would vary the Tribunal's findings.[8] Any such pre-clearance by the Tribunal would bind the Tribunal indefinitely.[9] The provisions in section 74 of the new Act grant the Director, not the Tribunal, the authority to render advance rulings. This procedure is preferable because an application before the Tribunal would most certainly result in a full-fledged hearing under s. 8 Competition Tribunal Act. Consequently, an expeditious and summary pre-screening mechanism would be, for all practical purposes, precluded. It is moreover uncertain on what basis the Tribunal (or the Director in the Competition Act) would have been obliged to make such a determination. Note that under the new Act, the Director may issue an advance ruling if he is "satisfied" that insufficient grounds to proceed under section 64 exist. It is submitted that this "test" is not helpful to the business community.

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[5] Ibid., S.45(1)

[6] Ibid., S.45(3)

[7] Ibid., S.34

[8] Ibid., S.45(3); Note: The section granted the Tribunal the discretion to issue a "conditional" pre-clearance, a discretion which is not available in Bill C-91.

[9] Ibid., S.45(4)

A second fundamental flaw in Bill C-256 is the failure to address the issue of subsequent changing economic circumstances. Section 45(4) should have included a limitation period on the duration of immunity from future proceedings under the merger proscriptions. It must be emphasized that the initiation of a pre-clearance application under Bill C-256 was absolutely voluntary on the part of the Commissioner. Parties which contemplated a merger which would lie below the large merger threshold enunciated in S.32(1) would run the risk of proceedings if they opted to avoid the advance ruling procedure. On the other hand, transactions which would surpass the large merger threshold were required to be evaluated by the Tribunal and to be subsequently permitted, disallowed or presumptively allowed at the expiration of one year from the date of registration. Although this "waiting period" would appear excessive,[18] the fundamental concept in the registration provisions in Bill C-256 formulated the pith and substance of the pre-notification provisions in the Competition Act, excepting, of course, the information requirements.

(c) Early Guideline Provisions

A provision in Bill C-256, which has not reappeared in any subsequent proposals to the competition laws entitled the tribunal on its own initiative, or at the request of the Minister of Consumer and Corporate Affairs, to formulate draft guidance rules which, after public discussion, could be adopted as guidance for the persons in the industry but would not be binding on either the Commissioner or the tribunal. A similar provision would not be necessary if the new merger provisions contemplate the use of merger guidelines similar to those in use in the United States. Although it would appear that no legislation is needed for an administrative body to establish its own procedural rules, guidelines might be construed as approaching substantive law too closely. To be safe, the Governor in Council should pass a regulation pursuant to s.100 Competition Act which would permit the Director to establish these standards. A caveat must be placed early on such guidelines; the prosecutorial body, not the adjudicative tribunal, must be granted the responsibility of formulating and utilizing such guidance rules. These Guidelines could be useful to the Director under the new Act in his predetermination of whether to initiate an action under the substantive merger provisions or to apply to the adjudicator for an interim injunction.

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[18] See: R.J. Roberts and C.A. Hewat, "Pre-merger Notification in Canada", (1986) 11 Canadian Business L.J. 135, at p. 140.

2. THE SKEOCH-MCDONALD REPORT

(a) The Hybrid Advance-Clearance Provision

In 1976, the Skeoch-McDonald Report envisoned an advance clearance procedure for mergers and rationalization agreements. As an aside, the authors alluded to the partial protection that could be available to control the behaviour of large mergers through the use of effective monopoly provisions. However, the Report stated "controls on misuse of market power are not an adequate alternative to a merger that looks bad from the start."[11] The Report recommended a process that was triggered by the parties themselves and was regulated by statutory limitation periods.

> A written application for advance clearance would be made to the Director by the firm or firms involved. The Director would have 30 days from receipt of the application to decide whether or not to hold an inquiry. During that period he might, subject to

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[11] Skeoch-McDonald Report, p. 337

> requirements of confidentiality, wish to consult other government agencies such as the Departments of Finance or Industry, Trade and Commerce or personnel in more specialized functions such as regulatory boards. He might also request additional information in writing for the purpose of making his decision. The proposal would be deemed to be approved at the expiry of the 30 day period unless within that time the Director communicated to the applicant his intention to hold an inquiry, or else referred the matter directly to the Board for disapproval or for terms and conditions to qualify an approval.'[12]

The Director of Investigation and Research would be permitted to apply to the "National Markets Board" for a 60 day extension. A deeming provision precluded the Director from further proceedings before the Board if the Director opted not to hold an inquiry or to refer the matter to the Board within the 30 day (60 day extension) "review period". Again, the issue of balancing the limitation period which would activate the deeming provision must be addressed. Sufficient time must be allowed for the Director to compile and evaluate the relevant economic information while reasonable protection must be afforded the merging parties so that the transaction will not be terminated before it has started. The advance clearance proposals in the Skeoch-McDonald Report went to great lengths to incorporate and be compatible with the provisions of the then Foreign Investment Review Act (re-enacted as Investment Canada Act). Several difficulties arose when attempting to coordinate the two Acts. First, the Director of Investigation and Research was prevented from using only FIRA information to initiate and inquiry. Second, the Director was forced to assume that Cabinet would approve the foreign acquisition, otherwise the Director would not have had reason to believe an offence under the Combines Investigation Act (1976) was about to be committed. Despite section 5(3) of the Foreign Investment Review Act, the effect of Cabinet approval of a foreign merger on proceedings under the merger provisions of the Combines Investigation Act (1976) was uncertain. Finally,

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[12] Ibid., p. 337-338

> The basic difficulty in harmonizing the procedures under the two statutes stems from the fact that for all intents and purposes under the Foreign Investment Review Act a merger cannot take place unless and until specific approval is given. This results in special time pressures.[13]

The Report recommended that:

> [T]he matter not proceed to cabinet until the evaluation under the Combines Investigation Act is completed. In part this choice follows from our view that as a matter of law a cabinet decision approving a merger application under the Foreign Investment Review Act should insulate the persons involved from further merger proceedings under the Combines Investigation Act. Unless the cabinet decision were delayed some foreign mergers would not be evaluated with the degree of thoroughness with which domestic mergers were evaluated, and disparate treatment would not be desirable.[14]

The difficulty with such a procedure was that nothing required the parties to apply to the Director of Investigation and Research for an advance clearance.

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[13] Ibid., p. 340

[14] Bill C-42, S.31.71(9),(10),(11)

Although the objective of the Report to subject foreign mergers to the same scrutiny as domestic mergers is commendable, there was nothing in the advance clearance recommendations that would require the potentially merging firms to subject their proposed transaction to a pre-merger review. The Report's pre-screening suggestions appear to be a hybrid provision, incorporating the permissive triggering characteristics of an advance ruling section (See: Bill C-256, *supra*) and the mandatory deeming provisions of a pre-notification provision (See: Competition Act, *infra*) requiring the Director to either challenge the merger or acquiesce in its acceptability.

The advance clearance provision did consider the effect if the parties did not apply. Conversely, the provisions did not anticipate the bureaucratic nightmare if all sizeable transactions were submitted. Furthermore, the submission of information, which was required by the Director to determine the case, was voluntary on the parties.

3. BILL C-42 AND BILL C-13

(a) The Pre-Clearance Provisions of Bill C-13

To the surprise of most merger watchers, Bill C-42 deliberately omitted any form of pre-clearance or pre-notification provision, although it did partially address the FIRA compatability problem.[14] However, its relative, Bill C-13, did incorporate a provision paralleling the general discussion in the Skeoch-McDonald Report pertaining to the matter of advance clearance. Section 31.71(19) of Bill C-13 is for all intents and purposes identical to the advance ruling certificates provision proposed in S.74(1) of the Competition Act:

> Where the Competition Policy Advocate is satisfied by a party or parties to a proposed merger that he would not have sufficient grounds on which to apply to the Board under this section for an order in respect of such proposed merger, he may issue a certificate to the effect that he is so satisfied, on the evidence that such party or parties have placed before him.[15]

Once he issues a certificate, Section 31.71(20) bars the Competition Policy Advocate (Director) from applying to the Competition Board unless there has been a failure to disclose material facts, or he is required to conduct an inquiry by virtue of an application of six persons or the Minister of Consumer and Corporate Affairs and such inquiry discloses grounds for an application before the Competition Board.[16] The Competition Act version simply precludes the Director from making an application on substantially the same information.[17] Although both Bill C-13 and the new Act contain a limitation period, only Bill C-13 incorporates what could be described as an acceptability deeming provision or decision limitation. Bill C-13 limits the Competition Policy Advocate to 6 months[18] from the date of notification of the merger by the parties to determine whether or not he will proceed with an application before the Board or the transaction is deemed accepted; the new Act contains no such limitation on the time period allotted to the Director of Investigation and Research to decide on whether or not a certificate should be granted although under s.74(2) the Director must consider the request as expeditiously as possible. However, once a certificate is issued under the Act, the Director of Investigation and Research is prohibited from making an application before the Tribunal if the merger is completed within one year of the date the certificate is issued.[19] It would seem appropriate that a pre-clearance provision should embody both time limitations: a limit on the time in which the Director must determine whether or not he has sufficient grounds to apply to the Tribunal, and secondly, a temporal restriction on the parties to the merger requiring consummation of the transaction. The general three year limitation period pursuant to section 69 of the new Act is only operative once the merger has been completed. It would not induce the Director to consider expeditiously the advance ruling application. Neither would section 75 Competition Act have this effect. Its purpose is to create an incentive on the merging parties to complete the transaction within one year after the certificate has been issued. Although the Director, pursuant to s.74(2) Competition Act, is under obligation to proceed expeditiously to consider advance clearance, no sanction operates if he does not.

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[14] Bill C-42, S.31.71(9),(10),(11)

[15] Bill C-13, S.31.71(19)

[16] Ibid, S.31.71(20)

[17] Competition Act, S.75

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[18] Bill C-13, S.31.71(21)(22); Note that upon application by the Competition Policy Advocate to the Board, the limitation period may be extended to 12 months. Note: Under s.74(2) Competition Act, "The Director shall consider any request for a certificate under this section as expeditiously as possible."

[19] Supra, n.17

In passing, it should be noted that under Bill C-13, the onus was placed on the Competition Policy Advocate to specify the information he requires. If he were to misjudge the situation and misdirect the parties respecting what information was to be submitted, he might not have been accorded any recourse. If material facts had been withheld, however, section 31.71(23) created an exemption to the 6 month limitation within which the Competition Policy Advocate might have applied to the Board. The Competition Act takes a more practical approach to this problem by shifting the onus onto the parties to supply all pertinent information. The discovery of new or unrevealed facts by the Director would override the prohibition on applying to the Tribunal after a certificate had been issued.

No mention was made in Bill C-13 to pre-notification provisions.

(b) The Royal Commission's Response to Bill C-13

The Report of the Royal Commission on Corporate Concentration was critical and extremely skeptical of the pre-clearance procedures codified in Bill C-13. First, the Competition Policy Advocate (Director) could conceivably be asked to rule on every possible merger. Although this concern has been avoided in the pre-notification provisions of the Competition Act, it is still quite plausible that the Director of Investigation and Research would be inundated with applications for advance ruling certificates simply as assurance for the parties against future proceedings. The fact that these rulings are discretionary does not preclude the onslaught of applications. Secondly, the requirement of information to be submitted to the Competition Policy Advocate (Director) will prolong the decision-making process to six months after all information has been received by the Advocate. As the Royal Commission warns:

> It would be impossible, of course, to specify completely and precisely in the statute the information the Competition Policy Advocate should have before he makes his decision. Presumably the information would be broadly that which would be put before the Competition Board if the merger were to be reviewed by the Board. The Advocate will be doing informally essentially what the Board would do formally.[28]

The new Act has attempted just such a detailed reporting scheme. Thirdly, the Competition Policy Advocate (Director) may have a latent bias against approving a proposed merger because he may wish to retain the option of proceeding to a trial on the merits. This bias has not been eliminated in the provisions contained in the new Act. Lastly, Bill C-13 allowed subsequent review by six persons (pursuant to S.7 Combines Investigation Act (1976)) or the Minister of Consumer and Corporate Affairs (pursuant to S.8 Combines Investigation Act). The lack of finality in the Advocate's ruling, which would have done little to foster certainty and reliability in the legislation, was rectified in the Competition Act by eliminating the possibility of subsequent inquiries. The Royal Commission concluded that:

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[28] Report of the Royal Commission, p. 164-5

> Although we are sympathetic to the idea behind the clearance procedure, which we think is intended to facilitate desirable mergers, we fear that the unavoidable costs and delays in that procedure, the possibility that the Competition Policy Advocate may give an unfavorable ruling at the end of it and the uncertainty overhanging even a favorable ruling may destroy much of its value in the minds of corporate executives.[11]

(c) Interpretation Bulletins

Following the lead of Bill C-256, section 27.2 of Bill C-13 granted to the Competition Policy Advocate the authority to issue "interpretive opinions". Such guidelines could then be employed to structure an administrative test for determining whether the prosecutorial body would proceed with some form of application before the board or tribunal.

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[11] Ibid., p. 165

Such guideline authorization provisions were required to be consistent with any decision of the courts or adjudicative tribunal:

> 27.2(1) The Competition Policy Advocate may, from time to time, issue, in writing, interpretive opinions setting out the interpretation that he places on any word or combination of words contained in this Act.
> (2) Whenever, in the opinion of the Competition Policy Advocate, an interpretive opinion that he has issued pursuant to subsection (1)
> (a) is at variance with a decision of the Board or a court, or
> (b) is in any respect erroneous or deficient,
> the Competition Policy Advocate shall issue, in writing, a cancellation of such interpretive opinion.
> (3) Subject to subsections (4) and (5), an interpretive opinion issued by the Competition Policy Advocate pursuant to subsection (1) is binding on him in any application made by him to the Board under Part IV.1.
> (4) An interpretive opinion that is at variance with a decision of the Board or a court thereupon ceases to be binding on the Competition Policy Advocate.
> (5) An interpretive opinion that has been cancelled by the Competition Policy Advocate on the ground that it is in any respect erroneous or deficient ceases to be binding on the Competition Policy Advocate in respect of acts or omissions occurring more than six months after publication of the cancellation thereof in accordance with subsection (6).
> (6) Every interpretive opinion and cancellation of an interpretive opinion issued by the Competition Policy Advocate pursuant to subsection (1) or (2) shall be published in the Canada Gazette.[22]

It might be advisable to consider such a provision for any new competition legislation in the light of their lawfulness and usefulness in tax law and the present Director's avowed intentions to foster voluntary compliance.

4. THE EMERGENCE OF "TRUE PRE-NOTIFICATION PROVISIONS"

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[22] Bill C-13, S.27.2

(a) The 1981 Proposals

The 1981 Proposals were first to publicly postulate a mandatory pre-clearance procedure which would require extremely large mergers to pre-notify the Director of their intentions.[23] The Director of Investigation and Research would then be given a short time period (sixty days) to analyze the merger, during which time the merger would be held in abeyance. At the expiration of the sixty day period, the merger would be deemed approved by the Director of Investigation and Research unless he notified the parties that he intended to oppose the merger. The 1981 Proposals also inaugurated the concept of a reporting threshold which would trigger the obligatory filing of a pre-merger notification "where a merger would result in an extremely large new enterprise in terms of annual sales or assets, or where an enterprise already of that extremely large size was making additional acquisitions."[24] Conglomerate mergers were to be exempted from such compulsatory provisions. It was anticipated that:

> The reporting threshold would represent a compromise between the need from a public policy viewpoint to have pre-notification and review of very large, potentially significant and complex mergers, and the desire to interfere as little as necessary with the decision-making process of firms in the market and to avoid placing additional reporting burdens on smaller

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[23] 1981 Proposals, n.21 at p. 7

[24] Ibid.

firms.[25]

In its embryonic stages, the pre-notification proposals were mute on the issues of required information, conditional advance rulings and the merger consummation "waiting period". In addition, the 1981 Proposals did not address the effect of the provisions on mergers which fell below the reporting threshold or which applied for an advance ruling. The 1981 Proposals leave the reader with the question:

> Question 5: In the case of very large and complex mergers and acquisitions by extremely large firms, where a public policy case for requiring pre-notification as set out above is justifiable, what in your opinion should be the the threshold in terms of millions of dollars of assets or sales at which firms should be required to pre-notify acquisitions of competitors, customers or suppliers (e.g., $100, $300, $500 million)?[26]

(b) Bill C-29

In 1984, Bill C-29 separated the dual functions of pre-clearance and pre-notification into separate sections. The pre-clearance provisions found in section 31.791 were transcribed mutatis mutandis directly into section 74 of the Competition Act. The modifications included the adjudicatory body in the Competition Act was to be the Competition Tribunal, not the courts, and the grounds for "satisfying" the Director would be altered to conform with the corresponding test for unlawful mergers under the Act. It is submitted that the lack of a compulsory time limitation in which the Director of Investigation and Research would be required to determine whether a certificate would be issued, would grant an inordinate amount of discretion to the Director to delay the proposed transaction indefinitely. In addition, no provision has been included for the Director to grant a conditional advance approval. The bias to not approve the merger, which was of great concern to the Royal Commission, still remains to haunt the procedure. Most importantly, any party who is the slightest bit leery about the acceptability of his transaction would more than likely apply to the Director of Investigation and Research for an advance.

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[25] Ibid.

[26] Ibid., n.23 at p. 8

In the case of advance rulings under the Income Tax Act, the numbers are not inconsequential. Furthermore, Revenue Canada does not make a ruling on issues which involve a matter of fact. Invariably, the question of whether a proposed merger is likely to lessen competition substantially will involve a matter of fact. The consequences of numerous applications would be to augment public costs and transfer the practical adjudicative authority from the Competition Tribunal to the Director of Investigation and Research.

The pre-notification provisions in Bill C-29 were also generally incorporated into the new Act without major structural modifications. The 1985 Consultation Paper criticized the provisions in Bill C-29 as being much too complex for their intended objectives. In addition, the paper asserted that the definition of "operating business" was ineffectual and consequently superfluous and should be deleted.[27] Because, the paper reasoned, the Restrictive Trade Practices Commission would in almost all circumstances require the information delineated in the long form, it was urged that the short form of information reporting be expunged.[28] Concern was also expressed that the "waiting period" or decision limitation period imposed on the Director of Investigation and Research was too short and should be extended.[29] Finally, the 1985 Consultation Paper raised a valid consideration; the information requirements were expressed with such a degree of specificity to warrant their inclusion in Regulations pursuant to the Combines Investigation Act, 1976.[30] Other than the adjustment to redefine "operating business", none of the consultation paper's apprehensions were assimilated into the present Act.

C PRE-NOTIFICATION UNDER THE COMPETITION ACT

1. THE OBJECTIVES OF THE PROVISIONS

Mr. Mel Capp, Assistant Deputy Director of Policy

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[27] 1985 Consultation Paper, n.49

[28] Ibid., n.51

[29] Ibid., n.52

[30] Ibid., n.53

Analysis for the Department of Consumer and Corporate Affairs, in a speech at the Canadian Bar Association Meetings in August, 1986, set forth the principles of design of the Canadian pre-notification provisions. Mr. Capp offered five rationale for the judging the sections:

(a) To supply certainty and predictability in the law;

(b) To be "transaction neutral" respecting acquisitions, amalgamatious and combinations;

(c) To be capital-market neutral;

(d) To be self-enforcing - the only way the Director can stop the process is to apply for an injunction;

(e) To be instigated by the parties.

The provisions are a valant attempt to satisfy these design criteria. Excepting the second standard, the provisions go a long way to avoid incompatability with these criteria.

It is hoped that the Canadian provisions will be as successful as their American counterparts (Hart-Scott-Rodino Act) in directing businesses to consider the competition implications of transactions and fostering voluntary compliance.

2. THE GENERAL STRUCTURE

Stage I: Notifiable Transactions:

The pre-merger notification provisions in the Competition Act are extremely detailed and complex, embodied in seventeen sections. In cases where the parties are obligated to report, the transaction must be held in abeyance until the expiration of the "waiting period". During this waiting period, the Director of Investigation and Research, however, will not be under an obligation to either approve or challenge the merger.[31]

Stage II: Exemptions

Once it has been tentatively established that the transaction is of such magnitude as to be subject to the reporting conditions, the Act provides for an extensive "let-out" list of statutory exemptions. If the merger, although large, falls within one of the specified exclusions, there will be no obligation on the parties to supply the information requested in Stage III.

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[31] These reporting procedures follow the structural flowchart of the Hart-Scott Rodino Antitrust Improvement Act, 15 U.S.C. S.18a (1976), although the Canadian version includes more extensive exemptions in an effort to restrict the application of the reporting requirements to potentially severe anticompetitive mergers. The Hart-Scott Rodino Premerger Notification rules apply if: (1) the acquiring firm has assets or sales of $100 million or more and the acquired firm is in manufacturing and has annual net sales or total assets of $10 million or more; or (2) the acquiring firm has annual net sales or total assets of $100 million or more and the acquired firm is not engaged in manufacturing but has total assets of $10 million or more; or (3) the acquiring firm has net sales or assets of $10 million or more and the acquired firm has annual net sales of $100 million or more regardless of whether either firm is engaged in manufacturing. If (1), (2) or (3) apply then the size of transaction test must be applied, i.e., whether as a result of the transaction the acquiring firm would hold at least 15% or more than $15 million worth, of either the assets or voting securities of the acquired firm, or more than $15 million worth of both the assets and voting securities of the acquired firm.

If all of the above apply, the firms involved must not legally complete the transaction until notification has been accomplished and a 30-day waiting period has thereafter expired.

Stage III: Information Requirements

The party required to file information has an election to supply the short form or the long form. However the Director of Investigation and Research is afforded the prerogative of overriding the parties short form election. Where a short form filing is elected the "waiting period" is seven days; where the long form is used the "waiting period" is twenty-one days.[32] Both periods extend from the date a pre-notification certificate is filed by the required party with the Director of Investigation and Research. Failure to comply may result in an injunction under s.72 or a fine or imprisonment under section 42(2).

D THE 1986 PROVISIONS IN DETAIL

1. STAGE I: NOTIFIABLE TRANSACTIONS

(a) "Operating Business"

The first step in ascertaining whether the party to a proposed transaction must file is to evaluate the magnitude of the merger relative to the parameters established for notifiable transactions. The preliminary condition that must be satisfied requires the merger to involve an "operating business" defined as follows:

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[32] Except for share acquisitions, where the "waiting period" is ten days, or such longer period, not exceeding twenty-one days, as is required for the shares to be taken up.

> "operating business" means a business undertaking in Canada to which employees employed in connection with the undertaking ordinarily report for work"[33]

This definition is an obvious attempt to resolve the criticism voiced by the 1985 Consultation Paper regarding the definition of an "operating business" offered in Bill C-29:

> 31.8 (1) In Sections 31.81 to 31.894, "operating business" means a business undertaking in Canada to which employees employed in connection with the undertaking ordinarily report for work that
> (a) has assets in Canada that exceed ten million dollars, or such greater amount as may be prescribed, in aggregate value, determined as of such time and in such manner as may be prescribed, or
> (b) had gross revenues from sales in or from Canada that exceed ten million dollars, or such greater amount as may be prescribed, in aggregate value, determined for such annual period and in such manner as may be prescribed;[34]

The purpose of such a restriction is to avoid pre-notification requirements for acquisition of non-active businesses and "shelf companies". One may be left with a residual apprehension that certain umbrella and holding corporations may be able to circumvent the reporting procedures. However, the Act requires at least one party to a transaction to be an "operating business". This "operating business" could be an affiliate, as defined in section 2(4) Competition Act, of the holding company. Section 82(3) Competition Act applies the pre-notification provisions to the acquisition of a corporation that controls a corporation that carries on an operating business. Even though these types of transactions would still be caught, it is submitted that a more reliable pre-screening net should eliminate the "operating business" requirement entirely, and simply require unobtrusive large transactions to file the short form and then allow them to proceed with the agreement. The seven day "waiting period" is designed to have a de minimus effect on the commercial arrangements in any event. In conjunction with an innocuous merger, the parties could apply pursuant to section 74 of the Act for an advance ruling certificate. If granted by the Director these non-active business mergers would be immune from the reporting requirements.

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[33] Competition Act, S.80(1): NOTE: See Appendix C for a detailed flowchart of the pre-notification provisions.

[34] Competition Act, S.31.8(1)

(b) The "Parties Threshold"

Step two on the road to classifying the arrangement as a notifiable transaction is to ascertain whether the assets or revenues of the parties to the transaction, and their affiliates, exceed the "parties threshold" of four hundred million dollars:

> 81. (1) This Part does not apply in respect of a proposed transaction unless the parties thereto, together with their affiliates,
> (a) have assets in Canada that exceed four hundred million dollars in aggregate value, determined as of such time and in such manner as may be prescribed, or

> such greater amount as may be prescribed; or
> (b) had gross revenues from sales in, from or into Canada, determined for such annual period and in such manner as may be prescribed, that exceed four hundred million dollars in aggregate value, or such greater amount as may be prescribed.
> (2) for the purpose of subsection (1), with respect to a proposed acquisition of shares, the parties to the transaction are the person or persons who propose to acquire the shares and the corporation the shares of which are to be acquired.[35]

The "parties threshold" applies to the aggregate of all the parties to the amalgamation or combination. For greater clarity, subsection (2) ensures that the "parties threshold" of four hundred million dollars applies to the pre-merger aggregate of both the acquiring and acquired firm for a proposed acquisition of shares. It is sufficient to note at this juncture that the Act has opted for an absolute size threshold, rather than a market share threshold such as had been included in the substantive merger provisions of Bill C-42.[36] The implication is that the drafters of the bill for the purposes of pre-notification are concerned with conglomerate mergers, even though the substantive provisions contained in section 64 are aimed at horizontal and vertical mergers. It is submitted that it would be more appropriate to reconcile the two so that either the "parties threshold" measures horizontal and vertical mergers or the substantive merger provisions track conglomerate activity.

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[35] Competition Act, S.81; Note: "prescribed means" set by Cabinet. See, S.96. In the version of Bill C-91 on Second Reading, the "parties threshold" was set at $500 million. The Department expects a $500 million level to catch 300 mergers, the $400 million level to net 400 mergers. See: Legislative Committee Hearings, at p. 11:43.

[36] Bill C-42, S.31.71(2) discussion on the problems inherent in any threshold criterion, see: Stanbury, W.T. and Reschenthaler, G.B. "Reforming Canadian Competition Policy: Once More Unto the Breach". (1981), 5 Canadian Business L.J. 381.

(c) The "Transaction Threshold"

The third step in Stage I is to define the type of transactions which will be governed by Part VII, Notifiable Transactions and determine whether the "transaction threshold" has been surpassed. Four types of transactions are enumenated:

1. Acquisition of assets, s. 82(2),
2. Acquisition of shares, s. 82(3),
3. Amalgamation, s. 82(4), or
4. Combination, s. 82(5).

In general terms, the principal target objective is to monitor the size of the actual transaction either by setting a size threshold for the acquired firm in the case of an acquisition, or by creating a size threshold for the resultant commercial entity in the case of an amalgamation or combination.

Acquisition of Assets

If the proposed transaction is an acquisition by assets, the "asset transaction threshold" is surpassed whenever the acquired firm, which must be an "operating business", has assets or gross revenues from the sales generated from those assets exceeding thirty-five million dollars.[37]

Acquisition of Shares

If the proposed transaction is an acquisition by way of shares, several intermediate issues arise before the determination of the "transaction threshold". Initially, the proposed acquisition must be of voting shares, otherwise no pre-notification is required.[38] In addition, the "asset transaction threshold" must also be met: the aggregate value of assets or the gross revenue from sales generated from those assets must exceed thirty-five million dollars.[39] With the greatest respect, it would appear that some commentators have overlooked the "asset transaction threshold" for a proposed acquisition of voting shares.[40] Once these two preliminary determinations have been made, the requirements follow one of two routes depending on whether the acquired company is public or private. If the acquired company's shares are publicly traded, the acquiring firm will be subject to pre-notification if:

(a) the acquiring firm acquires more than twenty percent of the votes attached to all outstanding voting shares, or

(b) if the acquiring firm already owns twenty percent or more before the acquisition, the acquiring firm acquires more than fifty percent of the votes attached to all outstanding voting shares.[41]

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[37] Competition Act, S.82(2)

[38] Ibid., S.82(3)

[39] Ibid., S.82(3)(a). Note that the original version of Bill C-91 did not restrict the assets to Canada.

[40] Rowley, William "Merger and Pre-merger Notification" in Reaction: The Combines Investigation Act. Vancouver: The Fraser Institute, 1986, at p. 32, 37.

On the other hand, if the acquired company's shares are not publicly traded, the acquiring company will be subject to reporting if:

(a) the acquiring firm acquires more than thirty-five percent of the votes attached to all outstanding voting shares, or

(b) if the acquiring firm already owns thirty-five percent or more before the acquisition, the acquiring firm acquires fifty percent of the votes attached to all outstanding voting shares.[42]

In summary, the bill requires both the "asset transaction threshold" and the "voting share transaction threshold" to be breached before the notice and inform provisions in section 86 will be required to be met in respect of an acquisition of voting shares.

It is convenient to deal with the matter of planned ongoing acquisitions of voting shares at this point. Although the issue might correctly be included in the following Stage II analysis of exemptions, it is addressed here because of its restricted application to acquisitions of voting shares only. If a potentially notifiable acquisition of voting shares is proposed within three years of a prior notification and informing under section 86 in relation to the same section 82(3) limit, then the company is not under an obligation to re-comply with supplying the required information.

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[41] Competition Act, S.82(3)(b)(i)

[42] Ibid., S.82(3)(b)(ii)

> 87.(1) It is not necessary to comply with section 86 in respect of a proposed acquisition of voting shares where a limit set out in subsection 82(3) would be exceeded as a result of the proposed acquisition within three years immediately following a previous compliance with section 86 required in relation to the same limit.[43]

It would appear that the exemption would be available only for subsequent notifications in relation to acquisitions of the same acquired company, although this is not explicitly clear and unequivocal from the actual wording of the subsection. In other words, one notification of the same transaction is good for three years. The wording used in the subsection, in the case of acquisitions "in relation to the same limit", creates even more uncertainty when conjoined with the definition of the "voting share transaction threshold". In the case of a publicly traded company, if the prior acquisition resulted in control of votes attached to shares exceeding twenty percent,[44] then in order to be required to notify the subsequent transaction would have to exceed fifty percent of the outstanding votes. But this is not the "same limit"; consequently the exemption would be unavailable. On the other hand, if the initial transaction were less than twenty percent, then the pre-notification requirements would be inoperative and the subsection 87(1) exemption would be redundant. If the suspect phraseology were to refer to either subsection 82(3)(b)(i) or 82(3)(b)(ii) in toto, then in the instance of a public corporation, the acquiring firm with prior voting share holdings exceeding twenty percent[48] could in practice acquire one hundred percent of the acquired firm within three years of a previous compliance.

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[43] Ibid., S.87(1)

[44] Ibid., S.82(3)(b)(ii): thirty-five percent for a private company

It is submitted that the confusion over section 87(1) arises for two reasons:

(a) It is not clear that the section is to apply only in cases where the initial transaction was merely proposed,

and

(b) The section is vague as to whether the second transaction must be in essence the same as the first.

Informal discussions with the Department of Consumer and Corporate Affairs have indicated that the "over-under-over" rule in subsection 87(1) has been included to cover complex share transactions on the open market. If the acquiring firm notifies that it intends to exceed a limit as prescribed in section 82(3)(b), that limit is actually exceeded within one year, then the percentage of shares drops below the limit and is subsequently re-exceeded, no further notification is necessary. The limitation period on such a transaction is extended from one to three years when the same limit is exceeded.

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[48] Ibid.

Because section 82(3) applies to private as well as public corporations, the rationale for the "over-under-over" rule for publicly traded enterprises is suspect. However, if the subsection 87(1) is not interpreted in this fashion, the one year general limitation period in section 91 would have little application to share acquisitions; transaction neutrality between asset and share acquisitions would be violated. It does not appear to be policy justified to permit share acquisitions to give notice, not exceed the limit, then rely on a three year limitation period.

If an acquiring firm is obliged under sections 82(3) and 86 to notify and inform the Director of Investigation and Research of a proposed acquisition of voting shares and if it intends within one year to make future acquisitions of voting shares which would exceed the fifty percent limit, the acquiring corporation may elect to supply, at the time of the initial compliance, further detailed information of the future acquisition.[46] It would appear that a two step merger consisting of acquiring twenty percent then a further thirty percent would subject the future acquisition to less rigorous scrutiny under section 87(3) than if the acquisition were consummated in one transaction.

Amalgamations

The third type of proposed transaction is classified as a proposed amalgamation where at least one of the amalgamating companies carries on an "operating business". The continuing company, after merger, would be required to report if its aggregate value of assets or gross revenues from sales generated from such assets exceeded seventy million dollars.[47] A glaring omission in this section is the definition of amalgamation. It is submitted that reference should be made to the definitions found in the Canada Business Corporations Act[48] or the respective provincial legislation. Furthermore, a "take-over bid" may be accomplished by the acquiring company offering, as consideration, shares in the acquiring company. It is recognized that after an amalgamation there will be only one corporate entity, whereas with an acquisition two companies will remain. However, unless the management of the two companies is maintained separate and apart, the distinction is strictly a legal one, not economic. As as result, the merger by way of acquisition of shares may, in reality, be identical to a merger by way of amalgamation. Consequently, one is at a loss to reconcile the $35 million "asset transaction threshold" structured for acquisitions of voting shares with the $70 million post-amalgamation "asset transaction threshold" expounded for amalgamations. The "parties threshold" under S.81 has to be greater than $400 million in assets or gross revenues even in the case of an amalgamation. The "asset transaction threshold", requiring the continuing company to be greater than $70 million appears to be in direct conflict. If company A, with $400 million in assets and company B, with $1 million in assets merge by amalgamation, it would appear the transaction would be notifiable. A similar acquisition would not.

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[46] *Ibid.*, S.87(2)(3)(4)

[47] *Ibid.*, S.82(4)(a)(b). It must be emphasized that the "parties threshold" and "transaction thresholds" are calculated by including all *affiliates* as defined in subsections 2(b),(c),(d) Competition Act. Any subsidiary, owned 50% by the parent, are included.

[48] Canada Business Corporations Act, S.C. 1974-75, C.33, S.175 *et seq*.

Combinations

The fourth, and last, type of proposed transaction which might trigger a notice and information requirement is a proposed combination, other than through a corporation. At least one of the members must be an "operating business" and the post-merger combination must have assets or gross revenues from sales generated by such assets exceeding thirty-five million dollars.[49] Again, any affiliate of the parent is included in the threshold determinations. Joint ventures would be exempt from these provisions if they satisfied the following requirements:

> 84. A combination is exempt from the application of this Part if
> (a) all the persons who propose to form the combination are parties to an agreement in writing or intended to be put in writing that imposes on one or more of them an obligation to contribute assets and governs a continuing relationship between those parties;
> (b) no change in control over any party to the combination would result from the combination; and
> (c) the agreement referred to in paragraph (a) restricts the range of activities that may be carried on pursuant to the combination, and contains provisions that would allow for its orderly termination.[50]

Again, the difficulty of arbitrary thresholds arises; there does not appear to be an obvious public policy justification for requiring reporting for combinations which are only one half the post-merger size of similar amalgamations.

(d) Potential Problems

The fundamental precepts of the pre-notification provisions give rise to some lingering concerns when combined and integrated with the remainder of the Act. The practical purpose of the Stage I provisions is to identify which parties are required to notify and inform the Director of Investigation and Research of their merger intentions. Conceptually, it would appear that the Act is aimed at throwing the reporting net around absolutely large transactions. It is suggested that the notifiable transactions provisions will group these large mergers into a set which may or may not intersect with the potential set of mergers that will lessen competition substantially. Furthermore, even if the two sets do coincidentally intersect, some large but harmless mergers will be subjected to the reporting procedures, while other relatively small but potentially anticompetitive transactions will evade inspection. As a result of the discrepancy in defining the boundaries for notifiable transactions and reviewable mergers, the Act once again runs headfirst into the recurring theme that large transactions may be procompetitive in the relevant market and relatively small mergers may occasion substantial anticompetitive structural alterations. Unfortunately, the test of reviewable mergers in section 64 does not lend itself to simple pre-notification criteria. Therefore, if it is assumed that all mergers need not notify, some simple and practical form of cut-off test is desirable; to these ends, the "thresholds" defined in section 82 are appropriate. Moreover, these large transaction thresholds will monitor the accumulation of aggregate economic activity. The majority of large mergers which are competition neutral need only inform the Director; the Director may then acquiesce to the transaction.

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[49] Competition Act, S.82(5)(a)(b)
[50] Competition Act, S.84

Turning to the specifics of the Stage I requirements, one is once again compelled to query the rationale for choosing the specific absolute thresholds. It is not the purpose of this discussion to challenge the actual values employed in the Act for two reasons: first, that is a technical matter that must be accomplished by comparing the actual dollar value magnitude of current Canadian mergers with the size threshold deemed to be suspect; second, the value of the thresholds may be altered by cabinet approval. Tangentially, what should be noted is that the thresholds cannot in the future be amended downward by Cabinet. This would appear to render the Act restrictive in a period of deflation. More importantly, one must consider the level of each threshold relative to each other. The conjunctive effect of the "parties threshold" and the "transaction threshold" could conceivably allow an extremely large acquiring firm to embark upon a conscious policy of acquiring the entire subset of fringe firms and not be subject to the reporting provisions, just as long as each acquired firm fell below the "transaction threshold". In contrast, a small acquiring firm, in absolute size, could acquire another firm which exceeded the "transaction threshold" but not be required to file the requisite information if the four hundred million dollar "parties threshold" had not been exceeded. However, such an arrangement may certainly have economies ramifications in a particular relevant submarket. As well, one must question the rationale for defining the "transaction threshold" in terms of the aggregate value of assets, if the implied objective of the pre-notification provisions is to compile pertinent information to facilitate expeditious evaluation of potentially highly anticompetitive mergers. The relevant issue should be the actual or potential capability of the firm to produce substitutable products, not the value of the assets that are employed to generate such fungible goods. Lastly, there is no *a priori* guarantee that an acquiring firm which purchases twenty percent of a public company or thirty-five percent of a privately held corporation will achieve *control* of the acquired firm. *A fortiori*, the acquisition of twenty or thirty-five percent of the shares of a company which in turn controls another company with assets or revenues over thirty-five million dollars may perhaps even weaken further the degree of actual control necessary to trigger the filing requirements. Similarly, the purchase of assets exceeding thirty-five million dollars from an acquired company with total assets of four hundred million dollars may neither transfer any *control* to the acquiring firm nor affect the residual competitiveness of the slightly smaller firm from which the assets are purchased. If one assumes that the only requirement for notification should be "bigness", then these criticisms are of no concern. On the other hand, if in addition to absolute size, one attempts to capture other factors which may trigger the need for the Director to be informed, then these issues are relevant.

In summary, ignoring for the moment the specific criticisms of the proposed sections, an absolute threshold to require pre-notification has the advantage of simplicity, understandability and applicability to the business community. In addition, if public policy were to be redirected towards political and international concerns rather than domestic market share evaluations, an absolute size barrier would be quite acceptable. The social cost of this form of test would be measured in the additional costs to those firms which were required to report but were not eventually subject to proceedings. The alternate approach of employing a notifiable transactions test which utilize a market share structural test or lessening competition substantially test would, by definition, necessitate a predetermination by the firms of the relevant market or the resultant anticompetitive effect. Although this might ultimately result in a more precise determination of the firms that should report, the unpredictability, unreliability and impracticality to the economic community would far outweigh any precision benefit. It is thus recommended to proclaim, mutatis mutandis, the absolute size reporting thresholds as soon as the Competition Tribunal can be constituted. Once it has been determined that the proposed transaction is also a notifiable transaction, the second major stage must address whether or not the agreement falls within a select group of limited exemptions.

2. STAGE II: EXEMPTIONS

(a) Specific Exemptions

A eclectic grouping of notifiable transactions are expressly exempted from the requirement to notify and inform. For the most part, the majority of these exclusions are contained in section 83 pertaining to acquisitions, section 84 exempting joint ventures and section 85 setting forth general exemptions.

The first subgroup of six exemptions, which are applicable only to the acquisition of assets or voting shares, are exempt from the application of Part VII:

> Exemptions
> Acquisitions of Voting Shares or Assets
>
> 83. The following classes of transactions are exempt from the application of this Part:
> (a) an acquisition of real property or goods in the ordinary course of business if the person or persons who propose to acquire the assets would not, as a result of the acquisition, hold all or substantially all of the assets of a business or of an operating segment of a business;
> (b) an acquisition of voting shares solely for the purpose of underwriting the shares, within the meaning of subsection 4.1(2);
> (c) an acquisition of voting shares or assets that would result from a gift, intestage succession or testamentary disposition;
> (d) an acquisition of collateral or receivables, or an acquisition resulting from a foreclosure or default or forming part of a debt work-out, made by a creditor in or pursuant to a credit transaction entered into in good faith in the ordinary course of business;
> (e) an acquisition of a Canadian resource property, as defined in paragraph 66(15)(c) of the Income Tax Act, pursuant to an agreement in writing that provides for the transfer of that property to the person or persons acquiring the property only if the person or persons acquiring the property incur expenses to carry out exploration or development activities with respect to

> the property; and
> (f) an acquisition of voting shares of a corporation pursuant to an agreement in writing that provides for the issuance of those shares only if the person or persons acquiring them incur expenses to carry out exploration or development activities with respect to a Canadian resource property, as defined in paragraph 66(15)(c) of the Income Tax Act, in respect of which the corporation has the right to carry out those activities where the corporation does not have any significant assets other than that property.[11]

In this group, the first exemption excludes the notification requirements for purchases of real property or goods in the ordinary course of business. However, it must necessarily not exclude the acquisition of all the assets of a business because this is precisely the objective of Part VII. However, a difficulty may arise when one attempts to reconcile this exemption with the "asset transaction threshold" stipulated in section 82(2). If the acquiring firm purchases any of the assets of an operating business, the aggregate acquisition exceeding thirty-five million dollars, then the transaction must be reported. Yet, the "ordinary course of business" exemption would purport to exclude such an agreement if two conditions were satisfied. First, the acquisition must be accomplished in the "ordinary course of business". This condition allows for the purchase by large conglomerates of, for example, office equipment valued in excess of thirty-five million dollars. Second, the purchase must not be of substantially all of the assets of

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[11] Competition Act, S.83

the acquired firm or operating segment thereof. It is certainly conceivable that a take-over could be structured to acquire assets in a series of "insubstantial" purchases in the ordinary course of business. This "paper clip" exemption will undoubtedly be clarified by judicial interpretation; the intent of the exemption to excluded ordinary business purchases is relatively clear.

Exemptions from the pre-notification provisions for the purpose of underwriting, making an inter vivos gift or a disposition on death, or facilitating foreclosure, default or debt work-out are all justified on the grounds that the likelihood of any anticompetitive effect of such arrangements is nonexistent. In contrast, however, one is forced to question the appropriateness of resource exploration and development incentives[52] being included in an act, the primary purpose of which is to stimulate competition and economic efficiency. It would appear more equitable if no "chosen industries" were afforded special treatment within the Competition Act. If it is government policy to target specified sectors, such incentives could be more appropriately and effectively incorporated into the Income Tax Act.[53] It is submitted that economic theory does not support such tax expenditures; thus, similar competition incentives can only be justified on political grounds.

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[52] Competition Act, subsections (e)(f)

[53] Income Tax Act, R.S.C. 1952, c.148, as am. by S.C. 1970-71-72, c.63: See: p. 66(15)(c) for the definition of Canadian resource property.

(b) Joint Ventures

The Assistant Deputy Director, Mel Capp revealed in a speech to the Canadian Bar Association, August, 1986, that section 82(5) was a mere fiction to allow the subsequent exemption of joint ventures. Section 84 defines a joint venture as an unincorporated combination in which:

(a) All parties contribute assets;

(b) There is no change in control over the parties; and

(c) A termination date for the project is specified.

In comparison, Section 67 also defines a combination to include any person that is not incorporated. Much discussion on Second Reading of Bill C-91 centred around including incorporated joint ventures in the substantive exemption. In the case of the substantive section 64, this would create a loophole to circumvent the entire review procedure. One must realize that this section was included in the Act only after intense lobbying from the business community. On the other, this argument is not available for pre-notification. Incorporated joint ventures should still be required to pre-notify.

(c) General Exemptions

The general exemptions apply to any of the three types of notifiable transactions: acquisition, amalgamation and combination.[54] The first exemption, which excludes pre-notification for mergers of affiliates,[55] addresses the policy objective of stimulating industrial rationalization. One must recall that the arrangement may still be subject to scrutiny and prohibition under the substantive merger provisions of the Act. For example, in the K.C. Irving case it was argued that even though the newspapers were affiliated, they were competitors. The second general exemption is necessary to tidy up the Advance Ruling[56] provisions by eliminating the requirement on a pre-cleared merger to re-submit information. The third exemption is the general transitional section which permits mergers which have become legally binding before the assention of the Act and practically completed within one year thereafter. The subsection may give rise to some interpretative anomalies resulting from the use of the phrase "entered into". And finally, a residual general exemption allows future classes of transactions described by regulation by the Governor-in-Council to be exempted. This may merely be a "basket clause" to permit the inclusion of future class of exclusions. One must be warry that this exemption is not misused to create a "Cabinet override" of all the provisions in Part VII. All potentially anticompetitive transactions should be required to notify and inform the Director of Investigation and Research. The firm may certainly elect to submit the relatively uncomplicated short form information report. It is submitted that the political ramifications should be evaluated at the merger test stage, not at the notification stage.

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[54] Competition Act, S.85(a)(b)(c)(d)

[55] Competition Act, S.2(2)(3)(4) defines "affiliate", "subsidiary" and "control".

[56] Competition Act, S.86(1)

3. STAGE III: INFORMATION REQUIREMENTS

(a) Short and Long Form Filing

If the notifiable transaction is not exempted in Stage II, the person proposing the transaction must notify the Director of Investigation and Research that the transaction is proposed and supply the Director of Investigation and Research with specified information before the transaction is completed.[56] In the case of more than one person being obligated to file a report, each person is jointly and severally responsible.[57] In the case of a friendly merger, either party may report on behalf of both parties. In the case of a hostile takeover, either of assets or shares, only the acquiring firm will be a party to the merger and able to report. The person filing the notice is then afforded an election to submit the short or long form information;[58] however, if the person elects the short form this option may be overriden by the Director who may then require, within seven days of receipt of the short form, the long form information to be submitted. If the short form filing is submitted and accepted, the "waiting period" within which the transaction is not to be completed, is seven days;[59] if the long form filing is proffered, the "waiting period" stalling the merger is twenty-one days.[60] Both waiting periods may be shortened if the Director notifies the persons that he does not intend to challenge the merger under the substantive provisions. Both "waiting periods" may be extended by the Director obtaining a S.72 interim order or, in conjunction with a concurrent proceeding, a S.76 injunction. Although S.72 is specifically tailored for the pre-notification provisions, S.76 injunctions are not excluded (See: Chapter VIII).

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[56] Competition Act, S.86(1)
[57] Competition Act, S.86(2)
[58] Competition Act, S.92

The short form filing requires the person(s) proposing the transaction to supply the following information:

1. The description of the proposed transaction and the business objectives,
2. Copies of all legal documents,
3. The names and addresses of all parties,

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[59] Competition Act, S.95(a)

[60] Competition Act, S.95(b); if the proposal is an acquisition of voting shares to be effected through a stock exchange, then the waiting period is at least ten trading days, but not in excess of twenty-one days, as may be allowed by the exchange before shares must be taken up: S.95(c). This condition is necessarily to synchronize with the Securities Acts.

4. A list of their affiliates,
5. A statement of the parties' principal suppliers and customers,
6. A statement of assets and revenues,
7. Any filings with a securities agency, and
8. A financial statement as if the proposed merger had occurred previously.[61]

All of the above requirements are included in the long form filing under section 94, with the addition of detailed information related to the principal categories of products supplied or purchased. 1.

The names and business addresses of directors,

2. The principal categories of products produced and their sales,
3. The principal categories of products purchased and their total expenditure,
4. The voting shares held in other corporations,
5. A copy of every prospectus filed with a securities commission,
6. Any financial data prepared to assist the company in evaluating the transaction,
7. And similar information in respect of any affiliate, other than a wholly owned affiliate.

This list is extremely extensive; the breadth and detail of the requirements create an excellent opportunity for the Director to apply successfully for a preliminary injunction under section 72(1)(b) due to non-compliance with the pre-notification requirements. A difficulty arises in determining who is proposing the transaction. Expecially in cases of hostile take-overs, the acquiring firm may not have access to all the information required under sections 93 or 94.

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[61] Competition Act, S.93

(b) Shortcomings

The primary shortcoming of both methods of reporting rests with the paucity of pertinent information available to determine the ultimate issue - does the merger lessen competition substantially? It is suggested that the information upon which the Director could make an informed judgment respecting the anticompetitive effect of the proposed transaction must necessarily encompass the concepts embodied in the definition of the relevant market and the existence of possible barriers to entry. Although the additional information required under the long form filing may be of greater assistance the Director in such determination, it would certainly be the exception, rather than the rule, for the Director to be able to assess the impact of the transaction within a three week period. As a result, any suspicions on the part of the Director which were not resolved within the three week period would induce him to apply to the Tribunal for a section 72 interim order.

If one accepts the view that the Director is then obligated to commence proceedings,[41] the ultimate result would impose on the Director the liability of determining the anticompetitive effect of the proposal within at most twenty-one days. This obligation is further supported by the fact that the interim order must be obtained by proving a substantial lessening of competition is likely. The burden of collecting collateral information lying on the Director of Investigation and Research would render the process impracticable and unproductive. Furthermore, the request that the transaction be simulated by the parties in order to produce pro forma financial statements as if the transaction had taken place is fraught with possibilities for creative accounting. And finally, section 95 requires that the transaction "not be completed" until the obligatory waiting period has expired. The connotations to the word "completed" allow room for firms to negotiate, structure, draft and agree to an arrangement in principle, then notify the Director of Investigation and Research of the proposal only to wait at most twenty-one days for the formal execution of the documents. In the ordinary course of business dealings involving complex documents and a phalynx of legal advisors, twenty-one days to arrange the final meeting is not unusual in the least. Consequently, unless the Director of

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[41] Competition Act, S.74(6)

Investigation and Research has decided to challenge the proposal, the merger will be effected.

It is not clear from the Act whether section 95, which prohibits completion of the proposed transaction until the expiration of the "waiting period", intends to operate as an outright injunction prohibiting any further action or whether the intent is to permit ongoing activity to complete the deal, but hold the parties separate and apart. From the perspective of the business community, the latter would be preferable; from the viewpoint of the Director of Investigation and Research, the former may be more desirable. It is recommended that, assuming the interim injunction provisions contained in section 72 are effective, the "waiting period" should simply act as an order to hold separate and apart. In addition, the Stage III Information Requirements would appear to shelter a latent predilection on the part of the Director to opt for the long form filing. During the requisite "waiting period", the Director may also have a natural prejudice against approving the merger; otherwise he would find himself usurping the adjudicative function of the Competition Tribunal. If the Director does not approve the merger during the "waiting period", he has reserved his rights to apply for an interim order or subsequent section 64 proceedings.

Finally, although such a requirement might be difficult to implement in practice, it is recommended that the information be supplied to the Director of Investigation and Research as soon as it should have been available, having regard to the circumstances. This amendment might avoid propitious timing on the part of the companies required to file. Creative entrepreneurs and clever lawyers may have the transaction structured to irreversibly commingle the companies immediately following the "waiting period".

VII INJUNCTIVE RELIEF

A THE STATE OF THE LAW UNDER THE FORMER COMBINES INVESTIGATION ACT

Since the inception of modern competition policy, there has been and continues to be an ongoing interest in the applicability of injunctive relief to the merger process. Unlike policies to police conspiracies in restraint of trade or to curb abuses of dominant positions, merger policy is afforded the rather unique opportunity of arresting the transaction before serious harm to the economy develops. On the other hand, merger policy has been subject to the conflict all competition policy issues must face. The Canadian governments have endeavoured to minimize intervention in the large majority of inoffensive mergers and contemporaneously intended to block decisively anticompetitive transactions.

The timing of the remedy has proven to be crucial. Until the enactment of the 1976 amendments to the Combines Investigation Act, the remedies had included only ex post solutions such as divestiture and dissolution orders. However, by this stage the merger would likely be at an irreversible stage. Consequently, merger policy shifted emphasis to an ex ante direction; the design of competition policy was to stress the preventative rather than curative aspects of preserving competition.

The 1976 amendments addressed this temporal optimization problem by superimposing upon the prevailing Act a procedure for the obtaining by the Crown of a temporary abeyance in specified merger activity pending proceedings directed towards an ex ante prohibition order. The object of this provision was presumably to afford breathing space to the Director of Investigation and Research in order that he might institute proceedings to prohibit the merger, while ensuring at the same time that the transaction did not proceed beyond the point where an order for divestiture or dissolution would impose unrealistic difficulties. As noted by Muldoon, J., in the only jurisprudence respecting S.29.1 of the recently repealed Combines Investigation Act:

> Section 29.1 is aimed at not only suppressing the actual commission of any offence under Part V or section 46.1 of the Act, but also at forestalling the commission of any such offence.[1]

As an historical preface to the current provisions of the Competition Act, the landmark provision in the former Combines Investigation Act will be reviewed below. The purpose of this investigation is to outline the objectives of injunctive relief as it pertains to merger policy, to discover the difficulties contained in the former provisions and to place the new provisions of the Competition Act in context. This section of chapter VII will outline the law as it existed prior to the enactment of the Competition Act. Part B will highlight the inherent limitations under the former Act. And finally, Part C will review the development of the injunctive relief provisions prior to the new Act.

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[1] A.G. (Canada) v. Fleet Aerospace Co. et al. (1985), 27 March, T-494-85, Muldoon, J. (Federal Court-Trial Division) at p.7.

The final three Parts will focus on the new provisions, their common law basis in Part D, the provisions themselves in Part E, and a critique in Part F.

The injunctive relief provisions, embodied in section 29.1 Combines Investigation Act, may be artificially segmented for the purpose of clarity and discussion into the following six conceptual elements:

1. Notice of application;
2. Dispensation of notice;
3. Test for availability of remedy;
4. Duration of Injunction;
5. Duties of the Director of Investigation and Research, and
6. Non-Compliance with order.

Only one application, to be discussed in detail below, has been made under this section by the Attorney General of Canada and the application was dismissed. Therefore, it is imperative that a merger review mechanism which depends heavily on what might euphemistically be described as a legislative "DEW" line of advanced early warning and detection be capable of forestalling the transaction until the Director is able to review the circumstances and possibly institute substantive proceedings.

Notice, presumably by way of Notice of Motion, must be given to each person against whom the injunction is sought at least forty-eight hours prior to the hearing.[2] Where a court is satisfied that the forty-eight hour notice provision cannot reasonably be complied with or the matter is of such urgency that requiring service of notice would not be in the public interest, the court may dispense with service.[3] The above two provisions supply a dual approach to injunctive applications, contested or ex parte.

The substantive test to be employed by the courts in determining the availability of the interim injunction is a bipartite hurdle. The text of the fundamental provision follows:

> 29.1(1) Where it appears to a court, on an application by or on behalf of the Attorney General of Canada or the attorney general of a province,
> (a) that a person named in the application has done, is about to do or is likely to do any act or thing constituting or directed toward the commission of an offence under Part V or section 46.1 and
> (b) that if the offence is committed or continued
> (i) injury to competition that cannot adequately be remedied under any other section of this Act will result, or
> (ii) a person is likely to suffer, from the

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[2] Combines Investigation Act, S.29.1(2). See: Appendix C for flowchart.

[3] Ibid., S.29.1(3).

> commission of the offence, damage for which he cannot adequately be compensated under any other section of this Act and that will be substantially greater than any damage that a person named in the application is likely to suffer from an injunction issued under this subsection in the event that it is subsequently found that an offence under Part V or section 46.1 has not been committed, was not about to be committed and was not likely to be committed,
>
> the court may, by order, issue an interim injunction forbidding any person named in the application from doing any act or thing that it appears to the court may constitute or be directed toward the commission of an offence, pending the commencement or completion of a prosecution or proceedings under subsection 30(2) against the person.[4]

The Attorney General must first prove, on a balance of probabilities, that a person has done, is about to do or is likely to do an act which constitutes or is directed towards the commission of an offence under Part V (includes illegal mergers) or section 46.1 (non-compliance with an order).[5] The second half of the test requires proof of a more immediate detrimental nature which would precipitate the need for a temporary order to maintain the status quo. The Crown can elect to prove the necessity of an immediate and temporary remedy to avoid injury defined from either a macro-industry perspective or a micro-firm viewpoint. Relying on the former, the applicant must establish that, if the offence is committed, injury to competition which cannot be adequately remedied under any other section will result.[6]

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[4] Ibid., S.29.1(1)(a).

[5] Ibid., S.29.1(1).

[6] Ibid., S.29.1(1)(b)(i).

The latter option is directed towards the effect of the imminent transaction on an individual party; a person must be likely to suffer damage for which he cannot otherwise be compensated and such damage must be substantially greater than any damage which might result to a respondent subsequently found not to be in contravention of the Act.[7] If both the elements of the test are proved to the satisfaction of the court, it may issue an interim injunction forbidding any respondent from doing an act constituted or directed towards the commission of an offence, pending the commencement or completion of a prosecution or proceeding under the *ex ante* prohibition order provisions.[8]

The duration of the interim order depends upon two factors: whether an interim injunction has been previously issued and whether the present application is by way of notice of motion or *ex parte*? The normal case of a contested application would provide the courts with complete discretion to specify the period of time for which the order would be operative;[9] if the application were *ex parte*, the courts would be restricted to a ceiling of ten days.[10]

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[7] *Ibid*., S.29.1(1)(b)(ii); Note: This wording is an attempt to codify the Balance of Risk doctrine discussed *infra*.

[8] *Ibid*., S.30(2) sets out the test for obtaining an *ex ante* prohibition order by way of information.

[9] *Ibid*., S.29.1(4)(b).

[10] *Ibid*., S.29.1(3).

Additionally, if an interim injunction has been previously issued, either by way of notice of motion or ex parte, the courts may grant an extension for such definite period of time as stated in the order.[11]

As soon as an injunction has been granted, the Attorney General is under an obligation to proceed as expeditiously as possible to institute and conclude the proceeding.[12] Failure to comply with an injunction issued under this section would be punishable by a fine in the discretion of the court or imprisonment for a term not exceeding two years.[13]

The only judicial consideration of the interim injunction amendment to the former Combines Investigation Act was a decision rendered by Mr. Justice F.C. Muldoon of the Federal Court-Trial Division in A.G. (Canada) v. Fleet Aerospace et al.[14] The factual situation centered around a "take-over bid" by Fleet to the shareholders of Fathom, dated February 19, 1985. The shareholders of Fathom responded in such numbers that by the 19 March, 1985, the date of the application by the Attorney General, approximately seventy percent of the shares of Fathom had been acquired. This would certainly establish that there existed a concerted predisposition on the part of the shareholders of Fathom to view the "take-over bid" in a favourable light and to willingly sell their shares. In actual fact, the shares were being held in trust for the acquiring firm, Fleet, by two trust companies, Guaranty and National-Victoria Grey. The applicant was requesting an order forbidding the trust companies from releasing the shares to Fleet and requiring the two companies be held separate and apart until the commencement of proceedings under S.30(2) Combines Investigation Act or ten days, whichever came sooner.

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[11] Ibid., S.29.1(5)(a).
[12] Ibid., S.29.1(6).
[13] Ibid., S.29.1(7).
[14] The Attorney General of Canada v. Fleet Aerospace et al. supra, n.1.

The two protagonists, Fleet and Fathom, were in the business of manufacturing sonar handling equipment - the means of housing and deploying the electronic device. The housing equipment was available in two technical designs: the "hull-mounted" housing and the "towfish" style. The acquiror, Fleet, had been engaged in the manufacture of the towfish design for sale in the domestic market only; the acquired firm, Fathom, was involved in the development of the "hull" prototype in the domestic market and the "towfish" handling equipment for the foreign market. In addition, "[i]t appears that in recent times, Fathom has expressed to the Department of Supply and Services, some interest in supplying the towfish or variable depth type of sonar handling equipment"[15] in the domestic market. Muldoon, J. dismissed the application by the Crown for an interim injunction, stating, "the applicant has not presented clear and cogent reasonable and probable grounds for an injunction pursuant to section 29.1."[16] The discussion below is intended to highlight the shortcomings of the former provisions in order to place the provisions of the Competition Act in perspective and anticipate potential pitfalls.

B THE LIMITATIONS ON INJUNCTIVE RELIEF UNDER THE FORMER ACT

The provisions available for injunctive relief under the Combines Investigation Act were available for all offences under the Part V offences in relation to competition, or for section 46.1 contraventions of a court order. As a result of the general applicability of section 29.1 of the former Act, to both preliminary and final injunctions, the "time-metered procedural proceedings"[17] did not lend themselves easily to an exigent and temporary "holding pattern" while more formal proceedings might be instituted to prosecute or obtain a prohibition order pursuant to section 30(2) of the Combines Investigation Act. Because the procedures were not merger specific, the dispatch and flexibility which are peculiarly necessary to enjoin offending mergers in their incipiency were unavailable. In addition, the common law jurisprudence respecting the issuance of interim injunctions was relegated to a subordinate guidance role as a result of Parliament conferring upon the courts the extraordinary remedy available in section 29.1. These provisions, which were specifically enacted to deal with competition offences, were for the most part, self-contained proceedings:

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[15] Ibid., p. 17.
[16] Ibid., p. 21.
[17] Ibid.

> In such circumstances, the common-law jurisprudence will be invoked to fill in, or bridge gaps in the legislation, or to clarify any principle which seems to be necessary but incompletely discernible in the legislative text. Section 29.1 of the Combines Investigation Act, then, is a mini code of civil procedure. Counsel did not disagree in this: they accepted that the applicable tests upon which to uphold or reject the application are to be found in this code, with "guidance" only to be drawn from the common-law jurisprudence.[18]

In retrospect, some concern arises upon the expurgation of the common law jurisprudence respecting interim injunctions; the substitute and specialized "mini code of civil procedure" might have followed the same ineffectual path that the decisions assessing the substantive merger provisions under section 33 Combines Investigation Act had pursued. It would appear that Muldoon, J., in the Fleet case, relied heavily on analogy to the landmark K.C. Irving

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[18] Ibid., p. 7.

[1] decision, a merger situation which however did not involve any issue regarding the availability of injunctive relief. Such judicial superimposition of related but mutually exclusive legal doctrines elicits the suspicion that, possibly, the legislation providing injunctive relief should not delete the common law principles respecting injunctions completely. Retention of the jurisprudence governing the availability of provisional injunctions may have the effect of directing the courts away from the substantive merger law tests and towards the distinctive issues relating to injunctive relief.

The Parliament of Canada has not conferred the legislative endorsement to apply for an interim injunction on any person other than the Attorney General of Canada or the attorney general of a province. The parties to a merger arrangement, particularly the acquired firm, may certainly have valid reasons to temporarily enjoin the proposed merger and mitigate its own potential damages while an analysis is conducted of possible anticompetitive effects. The acquired corporation is definitely in the most advantageous position to know of the proposed transaction and to supply the court with the requisite information to adequately weigh the anticompetitive effects if the merger were to proceed unchecked. The possible restrictive and debilitating consequences on the acquiring firm if the merger were temporarily postponed could then be set forth by the respondent in reply to the acquired firm's application. Furthermore, it is not apparent why the ability of six citizens or the Minister[28] to initiate proceedings to enjoin a proposed merger are conspicuously absent from section 29.1 Combines Investigation Act. It is submitted that more universal access to provisional remedies should be integrated into the fledgling Competition Act.

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[1] R. v. K.C. Irving [1978] 1 S.C.R. 408.

Another preliminary matter which must be addressed before assessing the former substantive provisions under section 29.1 Combines Investigation Act is the constitutional validity question. This is a complex consideration, one which is not intended to be analyzed in great depth in this paper. In simplified form, the major constitutional arguments focus on three primary issues:

1. Does the Parliament of Canada have the constitutional jurisdiction under the Constitution Act 1867 to enact legislation to regulate competition?
2. If yes, are the injunctive provisions validly enacted procedural provisions?
3. Finally, if the former two questions are

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[28] See: sections 7 and 8 of the Combines Investigation Act for similar provisions to initiate investigative proceedings by the Director under the present Act.

> answered in the affirmative, do the procedures and chosen forum for adjudication conform to the Canadian Charter of Rights and Freedoms?

In the Fleet case, Muldoon J. dismissed perfunctorily any consideration that the procedures could be ultra vires:

> No party hereto has attacked the constitutional validity of section 29.1 of the Combines Investigation Act, apparently for good reason. It is, no doubt, a validly enacted procedural provision of a validly enacted law of Canada.[21]

As long as the courts adjudicate the dispensation of provisional injunctions, as is the case with section 29.1 Combines Investigation Act, it is likely that provisions will not run afoul of the principles laid down in several recent Supreme Court of Canada judgments.[22] The ratio decidendi of these cases required a complete separation of the investigatory and adjudicative functions under the legislation. However, any recommendation to shift the jurisdiction over provisional injunctive relief to an administrative tribunal must foresee and eliminate such overlap in advance.[23]

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[21] Supra, n.14, at p. 15.

[22] See: Hunter et al. v. Southam Inc. (1984), 14 C.C.C. (3d) 97 (S.C.C.).
Ziegler et al. v. Hunter et al., [1984] 2 F.C. 608. (Appeal)
Crain et al. v. Couture and Restrictive Trade Practices Commission et al. (1984), 6 D.L.R. (4d) 478 (Sask.Q.B.).

Turning to the explicit provisions themselves in section 29.1 Combines Investigation Act, notice of an application must be served on the affected parties unless such notice could not be reasonably complied with or the matter was of such urgency that the public interest would be better served by dispensing with service. One is compelled to stretch the bounds of ordinary commercial experience to fabricate a situation which would justify an ex parte issuance of a restraining order on an otherwise unsuspecting third party without affording the party the opportunity to enunciate and clarify his position. It is highly improbable that an act by the respondent, which would have prejudiced the ability of the Attorney General to remedy the outcome under any other section of the Act, could have been completed within forty-eight hours. Furthermore, it appears rather inequitable to have allowed the Attorney General to adduce evidence which would prove injury to a party if the injunction were not issued, while possibly omitting countervailing evidence to support the damages which would be suffered by the party against whom the injunction is sought but who might ultimately be successful under the substantive sections. Furthermore, the instant a "public interest" test is included in the elements to be satisfied in order to dispense with notice, an unnecessary and undesirable degree of equivocation and indeterminability are injected into the procedure. A fortiori, the "public interest" test emerges superfluent when read in the context of paragraph (3)(a):

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[23] This issue becomes imperative when structuring the injunctive provisions under The Competition Act, infra, n. 146 and accompanying text.

> (3) Where a court to which an application is made under subsection (1) is satisfied that
>
> (a) subsection (2) cannot reasonably be complied with, or
>
> (b) the urgency of the situation is such that service of notice in accordance with subsection (2) would not be in the public interest,
>
> it may proceed with the application ex parte but any injunction issued under subsection (1) by the court on ex parte application shall have effect only for such period, not exceeding ten days, as is specified in the order.[24]

It is submitted that a situation which is so urgent that it is in the public interest to dispense with notice to the respondent, is also a situation in which the forty-eight hour notice requirement cannot reasonably be complied with. In order to restrict the discretion in issuing ex parte orders, it might be advisable to delete the "public interest" option for dispensing with notice in s. 72(3)(b) of the Competition Act. The courts should deal with an ex parte application on a case by case basis, being required to be ever vigalent that the granting of such extraordinary remedies ex parte may deprive an "innocent" party of an opportunity to respond to the allegations.

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[24] Combines Investigation Act, S.29.1(3).

The essence of the interim injunction provisions under the former Act were embodied in a self-contained civil procedure which required proof of the elements by the Crown on a balance of probabilities. Such a burden of proof was definitionally less restrictive than the criminal burden of proof beyond a reasonable doubt which was applied to the substantive merger proscriptions. Consequently, the preliminary hurdle for assessing the acceptability of merger transactions would appear prima facie to have satisfied the implicit principle that the pre-screening test be less rigorous than the fundamental determining factors of legality. Muldoon, J., concurs in his reasons for judgment:

> Here, of course, the standard of proof beyond a reasonable doubt is not to be exacted of the Attorney General, because these non-criminal proceedings are brought pursuant to section 29.1 with a view to obtaining an interim injunction.[25]

However, to counterbalance the weaker burden of proof imposed on preliminary relief, the test itself required a greater effort to satisfy than the substantive test in sections 2 and 33 of the Combines Investigation Act. To obtain an interim injunction, not only must the Attorney General have established that an offence was or is likely to be effected, but in addition, that there was injury to an individual or competition as a whole which could not be adequately remedied otherwise under the Act. This additional obstacle may have had the effect of stultifying any comparative advantage the Crown might have initially enjoyed. One cannot help but wonder about the results if the substantive provisions monitoring potentially harmful mergers had also been subject to a civil burden of proof, as is presently the case in the Competition Act. If both preliminary and final relief are available on the civil burden of proof, then the only manner in which to construct injunctive remedies which would be more easily attainable than a final disposition would be to impose criteria for provisional relief which could be more easily established by the applicant. This could be accomplished by providing less elements in the offence or more restrictive requirements in the defences or exemptions. It does not appear that the Competition Act has accomplished either objective.

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[25] Supra, n.14, at p. 9.

The purpose of the entire merger section under the Combines Investigation Act was to prevent mergers which lessen competition to the detriment of the public. The parameters placed on the undesirable harm to be avoided were quite broad and encompassed the economic concepts of allocative inefficiency and social welfare loss. One must then question the appropriateness of allowing an interim injunction upon proof that an individual person has suffered non-compensatory damage. Both section 72 and 76 of the Competition Act have avoided this difficulty by deleting this criterion.

The availability of section 29.1 relief was inextricably linked with the commencement or completion of a proceeding for a pre-conviction [ex ante] prohibition order pursuant to subsection 30(2):

> (2) Where it appears to a superior court of criminal jurisdiction in proceedings commenced by information of the Attorney General of Canada or the attorney general of the province for the purposes of this section that a person has done, is about to do or is likely to do any act or thing constituting or directed toward the commission of an offence under Part V, the court may prohibit the commission of the offence or the doing or continuation of any act or thing by that person or any other person constituting or directed toward the commission of such an offence, and, where the offence is with respect to a merger or monopoly, direct that person or any other person to do such acts or things as may be necessary to dissolve the merger or monopoly in such manner as the court directs.[24]

It would seem, although this is by no means certain, from the phrasing found in subsection 29.1(1) that an interim injunction to enjoin a merger would have been available whether or not the Crown had already instituted an action for a prohibition order or a prosecution under Part V. The former provisions would have treated an application for an interim injunction in an identical fashion, regardless of whether the injunction application had been made prior or subsequent to the initiation of proceedings to deal with the transaction on its merits. It is submitted that the ability of the Crown to enjoin a merger, before possessing sufficient confidence in its case to commence formal proceedings, should be strictly constrained by statute, particularly with respect to the applicable test, the duration of the order and the provisions for extension. Otherwise, the provisional remedies could be misused to circumvent dealing with the issue on its merits. Additionally, the provisions could be employed to harass the business community.

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[24] Combines Investigation Act, S.30(2).

It is interesting to compare the procedural options that were available to the Director under the interim injunction provisions outlined in section 29.1 and the _ex ante_ prohibition orders which were enacted pursuant to section 30(2), Combines Investigation Act.[37] When applying for an interim injunction, the Director may have proceeded[38] to prosecute under Part V or to obtain an _ex ante_ prohibition order, but not both. Only after obtaining a conviction, might the Director have applied for a prohibition order under subsection 30(1). In contrast, when proceeding to obtain an _ex ante_ prohibition order, the

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[37] This perspective was originally discussed in: Nozick, Robert. "A Study of Prohibition Orders Under the Combines Investigation Act; A Strategy for Future Use". Unpublished Working Paper: University of Alberta, Faculty of Law, 1985, at pp. 28-30.

[38] See discussion _supra_.

Director was restricted to advance by way of information[29] only, not prosecution. Professor Nozick queries:

> A puzzling question arises from the wording in S.44(4) that in cases where S.30(2) is applicable proceedings may be instituted "...by way of an information under that subsection or by way of prosecution." The reference to proceeding by way of prosecution under S.30(2) seems to contradict the wording in S.30(2) itself that procedures must be implemented by information.[30]

The unavoidable conclusion is reached that a proceeding to obtain an ex ante prohibition order necessarily precluded any prosecution simultaneously under Part V:

> A possible interpretation of S.44(4) is that it simply emphasizes that while the Crown can proceed under S.30(2) it cannot also seek a criminal conviction if it does...But any other interpretation of S.44(4) necessarily implies the possibility of proceedings under S.30(2) by way of prosecution and not information; this would contradict the actual wording of S.30(2).[31]

The possibility existed that if the Director did not proceed to prosecute, he may have applied for either an interim injunction or an ex ante prohibition order. However, the elements to have been satisfied in order to obtain an interim injunction were more onerous than those for the prohibition order; consequently, there emerged an inherent incentive in the legislation for the Crown to avoid the use of the interim injunction section.[32] On the other hand, if the Director did proceed to prosecute, he was compelled to seek preliminary relief via the section 29.1 provisions as the prohibition order was unavailable.

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[29] For an explanation of this type of "information", which is not construed in the criminal law sense, see: R. v. Hemlock Park Co-operative Farm Ltd., [1974] S.C.R. 123 (S.C.C.).

[30] Supra, n.27, p. 29.

[31] Ibid., p. 30.

Furthermore, one interpretation of subsection 29.1(6) reproduced below gives rise to some concern:

> (6) Where an injunction is issued under subsection (1), the Attorney General of Canada or the attorney general of a province, as the case may be, shall proceed as expeditiously as possible to institute and conclude any prosecution or proceedings arising out of the actions on the basis of which the injunction was issued.[33]

Was the applicant under a positive duty to proceed to institute and conclude a prosecution under Part V or proceedings respecting an ex ante prohibition order? If the term "proceed" was construed by the courts to mean "actually originate" an action, then this may a priori have inhibited the applicant from proceeding under section 29.1; if the term was interpreted only to mean "advance towards" a prosecution or proceeding, then any advance inhibitions to apply for injunctive relief on the part of the Attorney General might be averted. Notwithstanding this uncertainty, inequity remained as a consequence of dealing with applications for interim relief in like fashion, irrespective of whether or not they were made preceding or following the commencement of a prosecution or proceeding under subsection 30(2). As will be discussed in greater detail below, this ambiguity has been transplanted into the Competition Act by way of section 72(6) and 76(3).

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[32] Note that it was possible to apply for both an interim injunction and a prohibition order if the Crown does not proceed to prosecute. See Fleet v. Fathom, supra, n.1.

[33] Combines Investigation Act, S.29.1(6).

The basic test to have been satisfied was subdivided into two independent options available to the Crown. What would appear to have been the more appropriate test was specified in paragraph 29.1(1)(a) and subparagraph (b)(i). Simplifying slightly for convenience, the Crown was obliged to prove, on the preponderance of evidence, that the respondent was likely to do an act that was directed toward an offence which, if committed, would result in injury to competition which could not adequately be remedied under any other section of the Act. Several difficulties become obvious when these sections are viewed in toto. First, the Attorney General was obliged to prove irrebuttably, not that injury to competition was likely, but that it would result. Secondly, the Crown was required to negate all alternative remedies available under the Act. Lastly, the applicant was confronted headon with the historically insurmountable task of evidencing injury to competition with all the attendant rigor required in defining the relevant market. In the Fleet case, Muldoon J. made a lengthy reference to Chief Justice

Laskin's judgment in the *K.C. Irving*[34] case respecting the presumptive effect on competition of monopolistic power; Muldoon J. then remarked in a puzzling fashion, "I cannot say that the Attorney General's evidence in this case so far misses the mark ~~as~~ that which appeared in the *Irving* case."[35] With deference, section 29.1 contained no requirement that detriment to the public be established. Furthermore, the determination of the possible anticompetitive effects of Fleet's "take-over bid" completely sidestepped the issue of the relevant market. Oddly enough, the court relied upon the evidence of an officer of the acquiring company to elicit evidence that the two protagonists were not competitors:

> If Fleet and Fathom be competitors at all, such status appears to be little more than embryonic at the present. If they be not competitors, then the definition of a merger is not engaged, and no offence is in the offing. Bruce William Gowan, Fleet's Secretary-Treasurer, in his affidavit cogently casts considerable doubt upon the applicant's proposition that they are, in fact, competitors.[36]

It is interesting to observe that the court completely ignored the effects of potential competition:

> In logic, it would seem that if Fathom were to come under the complete control of Fleet, as in about 45 days it could, then such competition as there is between them would be lessened, that is unless Fleet were to accord Fathom some real autonomy. Fleet's

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[34] *Regina* v. *K.C. Irving Ltd. and 3 other Corporations*, [1978] 1 S.C.R. 408, 32 C.C.C. (2d) 1, 29 C.P.R. (2d) 83, 15 N.B.R. (2d) 450 (Appeal to S.C.C.) at pp. 12-13.

[35] *Supra*, n.14, at p. 20.

[36] *Ibid*., p. 17.

> President and Chief Executive Officer, Anthony George Dragone, reiterates in his affidavit the text of the "Purpose of the Offer and Plans of Fleet" in its Offering Circular. No changes are immediately planned.[37]

It is submitted that the relevant intentions should have been those of the acquired firm, Fathom, and any non-Canadian manufacturers. Moreover, the analogy to what some writers consider a fatal flaw in defining competition in the K.C. Irving case cannot be ignored.[38] Professor Cairns argued that a present undertaking to hold the editorial boards separate and to guarantee their editorial autonomy would not refute the contention that future competition may have likely to have been in jeopardy.

This pitfall notwithstanding, having made a determination that Fleet and Fathom were at best only embryonic competitors, Muldoon J. concluded:

> On the material before the court, it is more speculative than reasonable and probable that the acquisition of shares will lessen competition in the near future.[39]

The court continued to add, parenthetically it is hoped, that:

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[37] Ibid., pp. 17-18.

[38] K.C. Irving case, supra, n.19; For a discussion of the difficulties in concluding that competition had not been lessened in this case due to evidence adduced that indicated editorial autonomy was to be maintained, see: J.P. Cairns, "Monopoly, Detriment to the Public and the K.C. Irving Case", (1981) 30 University of New Brunswick L.J. 167.

[39] Supra, n.14, at p. 18.

> In any event, it seems that if the Attorney General moves with diligence and determination under subsection 30(2), Fathom's position in the market will not be irrevocably prejudiced, if at all before the issue can be litigated, or at least before the commencement of the litigation.[48]

It is undoubtedly true that the acquisition of shares, in and of itself, would not lessen competition either in the present or the near future. Therefore, upon applying the jurisprudence emanating from consideration of the substantive merger provisions, the judgment in the Fleet case is consistent with the finding that no person has done an act constituting an offence under Part V. However, it is submitted that the alternative criteria contained in paragraph 29.1(1)(a) have not been adequately dispensed with by the court. Is the mere acquisition of shares an act which is about to or likely to be directed towards the commission of an offence? It is at this stage that the court should evaluate the effect of increased concentration in the relevant market and the degree of effective barriers to entry. It is submitted that it is not at all certain that the circumstances in the Fleet case would support a finding that the acquisition was not likely to contravene the provisions of paragraph 29.1(1)(a). The provisions found in sections 72 and 76 of the Competition Act do not alleviate these difficulties. The substantive test under s. 64 is incorporated in both provisional injunctive provisions of the new Act; the Tribunal must still grapple with the basic problem of defining the market.

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[48] Ibid., p. 18.

Turning to the secondary element under s. 29.1(1)(b)(i) which must have been proven by the Attorney General, Muldoon, J. appears to have placed great weight on the availability of an alternate adequate remedy under the _ex ante_ prohibition order provisions. However, if the Crown were to proceed by way of information under subsection 30(2), it would be precluded from concurrently prosecuting under section 33; this might certainly not be an "adequate" remedy from the point of view of the Director and the Attorney General. Moreover, the court deduced that the acquisition of shares by Fleet did not "irrevocably prejudice" the position of the acquired firm, Fathom, in the market place. The acceptance of this conclusion, however, is not automatic. Fathom was a widely held public corporation; the restoration of the shares to their original owners would not have been a simple routine task. Conceivably, the renumeration paid to the shareholders may have already been disbursed to an innocent third party. The acquisition of shares by Fleet and a possible subsequent divestiture order may very understandably affect Fathom's share price, the demand for its product, financing opportunities or management strategy. Although this may not have been the situation in the _Fleet_ case, potential victims of "take-over bids" often incur extremely high costs in efforts to ward off the merger.[41] It is perhaps naive to assume that while the merger of Fleet and Fathom is being effected, the remainder of the market competitors are not instituting counteractive measures which may, in themselves, irrevocably prejudice the status quo. It must be emphasized that the legislation protects injury to the acquired firm, which cannot be adequately remedied by any other means under the Act. In consequence, even if the court were to find that, on the primary grounds, the mere acquisition of shares was not directed towards an offence, it is suggested that the secondary element could be satisfied.

The preliminary injunction provisions under the Competition Act do not require the negation of alternate statutory remedies. In this context the amendments are a marked improvement over their predecessor. In contrast, the interlocutory injunctions under section 76 may borrow from the common law jurisprudence and require the negation of preferable alternatives.

Counsel for both the applicant and the respondents concurred that no evidence was to be adduced respecting subsection 29.1(1)(b)(ii) (damages to a specific person); consequently, Muldoon J.'s statement negating any irrevocable prejudice to Fathom must be treated as obiter

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[41] See: John Greenwald, "Let's Make a Deal", Dec. 23, 1985, Time 44.

dicta. If treated otherwise, the court's reference to no possible prejudice arising before the commencement of litigation would trigger fundamental concerns with respect to the mechanics and objectives of the injunctive relief provisions. There appears to be fundamental confusion surrounding the purpose of preliminary relief. Is the object to maintain the public interest in competition or is it to preserve the competitive position of the acquired firm? Although the secondary proof of injury subsection[42] was not invoked in the *Fleet* case, and although evidentiary hurdles similar to those encountered under subparagraph (b)(i) would have arisen in any event, the Crown would have been extremely fortunate to succeed. Pursuant to s. 29.1(1)(b)(ii) the applicant must forecast the resultant effect upon the respondent if the order is issued and the offence under Part V is not subsequently committed. The Attorney General must further prognosticate a "substantially greater" damage to the applicant than to the respondent *if* the application were to be rejected. In summary, the construction of the test for determining the viability of injunctive relief must cautiously avoid the peculiar trapfalls that have emerged from the jurisprudence which has considered the primary merger proscriptions. The Competition Act is not above criticism in this regard.

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[42] Combines Investigation Act, S.29.1(1)(b)(ii).

The matter of the duration of the original order does not appear to raise any serious obstacles. It is reasonable to limit an ex parte order to a relatively short period of time;[43] likewise, the commonly accepted rules for interim injunctions, which allow for reasonable discretion in determining the duration of an order sought by way of notice of motion, are also acceptable.[44] The procedure for extending the initial order, however, may have imposed undue prejudice on the respondents. Whether the original order was obtained by way of notice or ex parte, an extension may have been granted upon notice for a definite but potentially unlimited period of time:

> (5) A court that issues an injunction under subsection (1), at any time and from time to time on application by or on behalf of the Attorney General of Canada or the attorney general of a province, as the case may be, or by or on behalf of any person to whom the injunction is directed, notice of which application has been given to all other parties thereto, may by order,
>
> (a) notwithstanding subsections (3) and (4), continue the injunction, with or without modification, for such definite period as is stated in the order; or
>
> (b) revoke the injunction.[45]

Since an interim injunction pursuant to this section could have been granted prior to any prosecution being commenced, there existed a potential hazard that the merger could have been effectively scuttled by the Attorney General without the merits of the case being brought in toto before the courts.

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[43] Ibid., S.29.1(3).

[44] Ibid., S.29.1(4)(b).

[45] Ibid., S.29.1(5).

Under the new Act, the preliminary injunctive section supporting the pre-merger notification provisions expressly limits the duration of the order and precludes any opportunity to extend the period of the order. The interlocutory provisions under section 76 rely completely on the ordinary principles of law governing injunctive relief.

Counsel for the applicant in the Fleet case presented a draft order which embraced an innocuous lapse provision. The injunction would automatically terminate at the expiration of ten days or on the date of commencement of section 30(2) proceedings, whichever occurred first.

> 6. That paragraphs 1 through 5 of this Order shall be effective pending:
> a) the commencement of proceedings between the parties hereto instituted in the Supreme Court of Ontario pursuant to Section 30(2) of the Act; or
> b) ten days from the date of this Order, whichever is sooner;
> provided that upon the commencement of proceedings between the parties within 10 days of the date hereof by the Attorney General of Canada pursuant to Section 30(2) of the Act, then this Order shall remain in effect pending the trial or other disposition of such proceedings;[44]

If proceedings were instituted within the time limit, the injunction would stand until the disposition of the matter by the courts. One cannot help but notice that the lapse provision effectively applied a self-imposed time limitation on the Crown within which to initiate more formal proceedings. The greater risk of being denied the application due to the potential ability of the Attorney General to delay proceedings indefinitely had therefore been defused.

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[44] Supra, n.14, at p. 5.

The effectiveness of the preliminary injunctive measures in the former Combines Investigation Act to prevent the harmful, and often irreversible, outcome of certain mergers or proposed mergers was significantly eroded by the initial failure of the courts to recognize the primary objective of such interim remedies. Because the Combines Investigation Act, as a public law statute, should have as its fundamental goal the preservation of competition and the promotion of efficiency, the compensation of individual players within the economy should be of secondary importance. In addition, from the point of view of temporarily protecting the public interest, the burden of proof imposed on the Crown should be less onerous than under the substantive provisions. Moreover, the Attorney General should not be under any compulsion to prosecute. Conversely, if the Attorney General does decide to proceed, he should not be allowed to abuse the intent of the section to obtain, in effect, a final bar to the merger. With regret, it will be argued that, except for the matter of compensating individuals within the economy, the recent amendments in the

Competition Act do not fair well.

C PRE-1986 PROPOSALS TO AMEND THE FORMER INJUNCTIVE PROVISIONS

Invariably, most discussions examining contemporary competition policy find their genesis in the Economic Council of Canada's Interim Report on Competition Policy. As indicated in the Council's "new approach" to competition policy:

> It might be well to provide the tribunal with the power to issue interim injunctions to stay the "scrambling" of the assets of merging firms while the hearings were in progress. In the light of its early experience, the tribunal would specify a time limit within which it would bind itself to render decisions on mergers.[47]

Even at this rudimentary stage, the Council recommended that time limitations merger be imposed upon the adjudicative body (to determine issues). It is interesting to note that such lapse provisions were to be self-administered as opposed to statutorily required. Moreover, it is unclear from the preceding excerpt whether such time constraints were to apply to interim injunctions as well as the determination of the acceptability of certain mergers on their merits.

The first appearance in the proposals following the

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[47] Economic Council of Canada, Interim Report on Competition Policy, Ottawa: Queen's Printer, 1969, at p. 115.

Interim Report is found in section 47 of Bill C-256,[44] the text of which follows:

> 47.(1) On application by the Commissioner, the Tribunal may, by order, temporarily enjoin persons to whom the order is directed from
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> (a) proceeding with a merger;
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> (b) proceeding with any measure pursuant to or made possible by a merger, or
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> (c) commencing or continuing a trade practice in respect of which an order of prohibition may be made under section 37,
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> where it is satisfied that the Commissioner has obtained or may be able to obtain evidence on the basis of which the Tribunal could make an order of prohibition or dissolution with respect to the merger or of prohibition with respect to the trade practice and that it would be contrary to the public interest to allow the merger, measure or trade practice to be proceeded with, commenced or continued, as the case may be.
>
> (2) An application under this section may be made ex parte by the Commissioner or on notice to the parties to the merger or trade practice to which the application relates.
>
> (3) An order under this section shall
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> (a) be in such terms as the Tribunal considers necessary and sufficient to meet the circumstances of the case, and
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> (b) have effect for such period of time as the Tribunal therein prescribes.
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> (4) In prescribing a period of time for which an order under this section will have effect, the Tribunal shall have regard to
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> (a) the time required to bring the merger or practice that is the subject of the order before the Tribunal for a final

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[44] Bill C-256, "An Act To Promote Competition, to provide for the general regulation of trade and commerce, to promote honest and fair dealing, to establish a Competitive Practices Tribunal and the Office of the Commissioner, to repeal the Combines Investigation Act and to make consequential amendments to the Bank Act" First Reading: June 29, 1971, 3rd Session, Twenty-Eighth Parliament, 19-20 Eliz. II, 1970-71 [The Competition Act].

> decision, as to whether it should be prohibited or dissolved in the case of a merger or prohibited in the case of a practice; and
> (b) the convenience of the parties to the merger or practice.
>
> (5) The Tribunal, at any time and from time to time, on application by the Commissioner or any person to whom an order under this section is directed, notice of which has been given to the persons to whom the order is directed or the Commissioner and all other such persons, as the case may be, and having regard to the factors referred to in subsection (4), may by order
> (a) continue an order under this section, with or without modification, for a prescribed period, or
> (b) cancel such an order.
>
> (6) Where an order is made under subsection (1) by the Tribunal, the Commissioner shall, as soon thereafter as is possible, apply to the Tribunal for an order of prohibition or dissolution in respect of the merger or for an order of prohibition in respect of the practice to which the order under this section relates.

Although the section was not directed specifically towards mergers, they were given special attention. The substantive test in Bill C-256 set the stage for several subsequent two-part tests. First, the Commissioner (Director) was obligated to satisfy the Competitive Practices Tribunal that he had or was able to obtain evidence upon which the Tribunal "could" grant a prohibition order. The phraseology is suspect and cumbersome, but the fundamental objective was very similar in principle to the former S.29.1(1)(a) Combines Investigation Act. The second element of this two part test challenged the Commissioner to satisfy the Tribunal that it would be contrary to the public interest to allow the merger to commence or proceed. In subsequent proposals, this second condition has been further partitioned into public and private injury. Even at this early stage of development, the legislators were contemplating that applications could be made either on notice or ex parte.[49] However, no limitation on the duration of the order was implemented notwithstanding the reference cited above from the Interim Report.[50] In lieu of statutory limitation periods, the Tribunal was obliged to regard the time required to bring the merger before the Tribunal and the convenience of the parties for prescribing the effective period of the order.[51] However, since the Commissioner was under a positive duty to apply for a prohibition or dissolution order "as soon thereafter as is possible",[52] the Commissioner may have been effectively precluded from applying for an interim injunction unless he also intended to challenge the merger under the substantive merger proscriptions.[53] It would appear that this provision was weakened in the Competition Act by requiring only that the Director "proceed as expeditiously as possible". Notwithstanding the modifications made to the fundamental test, and the changes made to the forty-eight hour normal notice period, the ten day ex parte limitation period and the duty of the Director to proceed expeditiously, the provisions of Bill C-256 were incorporated by way of Bill C-

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[49] Ibid., S.47(2).
[50] Ibid., S.47(3)(b).
[51] Ibid., S.47(4).
[52] Ibid., S.47(6).
[53] Ibid., S.34.

227[54] into the Combines Investigation Act, 1976, and eventually into the current Competition Act.

At the same time that the initial interim injunction provisions were being included in the Combines Investigation Act, 1976, as section 29.1, the Skeoch-McDonald Report[55] was advocating revisions. The authors recommended that the substantive test for what they entitled "interim prohibition orders" should impose upon the applicant only a prima facie burden of proof. It is presumed that the exhortation of a less restrictive burden of proof in contradistinction to the more onerous burden of proof required for formal prosecution proceedings would facilitate the acquisition of temporary prohibition orders. As the Skeoch-McDonald Report asserts:

> Interim prohibition orders are also a necessary power for the Board so that it might act promptly in those cases where irreparable harm or serious inconvenience might otherwise result and a prima facie case for a remedy is established. For example, this power might be necessary to protect a person from immediate effects of a misuse of market power by a competitor, or to prevent consummation of a merger pending proper assessment.* On the other hand, interim prohibition orders can work serious inconvenience or harm and are granted without a full hearing of the matter. Accordingly we believe they should be reviewable by the courts.

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[54] Bill C-227, "An Act to amend the Combines Investigation Act and the Bank Act and to repeal an Act to amend an Act to amend the Combines Investigation Act and the Criminal Code", First reading, November 5, 1973, First Session, Twenty-Ninth Parliament, 21-22 Eliz. II, 1973.

[55] Skeoch, L.A. and McDonald, B.C. et al, Dynamic Change and Accountability in a Canadian Market Economy, Ottawa: Supply and Services Canada, 1976, at p. 302.

> * In some merger cases it would be sufficient to order that the businesses continue to be operated separately, and the assets remain separately identified, until the assessment of the merger has been completed.[56]

It is presumed that the authors intended such interim orders to be heard initially by the National Markets Board (the adjudicative tribunal) and that the Board's disposition be reviewable by the courts in some manner. It is not clear whether the Board's decisions were to be appealable, or simply reviewable. Although this was a moot issue for the former Combines Investigation Act, the current legislation, when considered by the House Legislative Committee, grapple with this point. An appeal to the courts could effectively substantiate the jurisdiction of the courts for that of the Tribunal.

The _Skeoch-McDonald Report_ also recommended that, contrary to section 29.1 _Combines Investigation Act_, interim prohibition orders be available for only a limited period:

> The Board should be able to issue interim prohibition orders on terms, but the orders should not endure for more than a limited period, such as ninety days, unless the case is exceptional. Limited duration of the order minimizes the risk of its being resorted to as a cover for administrative inefficiency in the Department.[57]

Although the ninety day limitation period was probably too generous and subsequently has been shortened in the Competition Act, the authors recognized that the availability of such remedies could be misused to delay possibly innocuous transactions.

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[56] _Ibid_., p. 302.
[57] _Ibid_., p. 303.

Bill C-42, given First Reading in 1977, added another permutation to the expanding toolchest of concepts available to deal with interim injunctive relief. The text of the proposed amendment to section 29.1 Combines Investigation Act follows:

> 29.1(1) Where it appears to a court, on an application by or on behalf of the Attorney General of Canada or the attorney general of a province that a prima facie case has been presented to the effect that a person against whom an injunction is sought has done, is about to do or is likely to do any act or thing constituting or directed toward the commission of an offence under Part V or section 46.1, and that serious injury to competition or to the business of another person is thereby threatened, the court may, by order, enjoin that person from doing any act or thing that it appears to the court may constitute or be directed toward the commission of such an offence, pending the commencement or completion of a prosecution or proceedings under subsection 30(3) against the person.[38]

Although reviewable trade practices proscribed in Part IV.1 would be heard by the Board,[39] interim injunction applications relating to such practices, including mergers, would go directly before the courts. The practical result of such a procedure would be to greatly attenuate the role of the Board when disposing of the issue on its full merits pursuant to section 31.71 of the bill. Moreover, the use of the word "appears", in contrast to "satisfies" to convey the burden of proof, is rather ambivalent. It seems doubtful that the inclusion of the a prima facie onus would have any measureable impact on the application of section 72 or 76 of the Competition Act; these sections are already subject to the civil burden of proof on the balance of probabilities. The first part of the basic test incorporated similar phraseology to that being employed at the time in the Combines Investigation Act:

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[38] Bill C-42, "An Act to amend the Combines Investigation Act and to amend the Bank Act and other Acts in relation thereto or in consequence thereof", First reading: March 16, 1977, Second Session, Thirtieth Parliament, 25-26 Eliz. II, 1976-77, S.29.1(1).

[39] Ibid., S.31.71(3); Mergers were to be redefined under Part IV.1.

> [T]hat a person...has done, is about to do or is likely to do any act or thing constituting or directed toward the commission of an offence under Part V or section 46.1...

The second part of the former test was, however, simplified. The Crown was not compelled to negate all other remedies; the applicant was only required to prove serious injury either to competition or to another business. As a result, the expected difficulties associated with subsection 29.1(1)(b)(ii) would have been evaded. One must wonder when a merger would not threaten to seriously injure the business of another person, if that other person were the acquired firm? This would be an extremely difficult test to satisfy; the firms could comingle assets, particularly those facilities employed for research and development, for the benefit of the "business" of the acquired firm.

Furthermore, in evaluating whether the provisions for injunctive relief under Bill C-42 were an improvement over those of the Combines Investigation Act, notice must be take that the former required the Board to follow the principles applied by the Federal Court respecting injunctions, while the latter omitted such restrictions. Did this omission imply that because the application was before the courts in any event, the general principles regarding injunctions apply or did it implicitly permit the section to be construed as a mini code of civil procedure for which the general principles would only act as a guide? Muldoon, J., in the Fleet case, supra, invoked the latter interpretation. Bill C-13, the subsequent proposal to Bill C-42, seemed to invite the former interpretation by including in section 29.1(1) the phrase, "acting on the principles applied by that court in respect of injunctions."[60]

Appearing as an aberration in the general trend towards greater reliance upon the use of interim injunctions as a necessary component of merger monitoring, the Report of the Royal Commission on Corporate Concentration advocated the abolition of the injunctive provisions.[61] Although the authors do not address the issue directly, the report would appear to implicitly deprecate the use of interim orders due to their ex ante nature:

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[60] Bill C-13, "An Act to amend the Combines Investigation Act and to amend the Bank Act and other Acts in relation thereto or in consequence thereof", First reading: November 18, 1977, Third Session, Thirtieth Parliament, 26 Eliz. II, 1977, S.29.1(1).

[61] See Canada. Report of the Royal Commission on Corporate Concentration. Ottawa: Supply and Services Canada, 1978, p. 160 for a discussion.

> For all these reasons, we think that the competition law should deal in a prohibitory way with proven anticompetitive conduct and, correspondingly, that corporate mergers should not be subject to a review process or require official approval or consent before they are completed. Our conclusion carries with it a risk that, if there is a merger that has a significantly harmful effect on competition, the law will be able to deal with it only after the fact. We think this risk is slight.[62]

The entire issue of preliminary relief was completely disregarded in the 1981 Proposals[63] and did not reappear until the third draft of the Stage II amendments in 1984.

Bill C-29[64] was landmark legislation introducing the procedure for dealing with injunctive relief subsequently embodied *mutatis mutandis* in Bill C-91 and the Competition Act. The major distinction between the Bill C-29 and the Competition Act is:

1. Bill C-29 refered the matter of injunctive relief to the courts while the Competition Act utilizes the Competition Tribunal at

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[62] Ibid.

[63] 1981 Proposals. Canada. Department of Consumer and Corporate Affairs. Proposals for Amending the Combines Investigation Act: A Framework for Discussion. Ottawa: Supply and Services Canada, 1981.

[64] Bill C-29, "An Act to Amend the Combines Investigation Act and the Bank Act and Other Acts, in consequence thereof", First Reading: April 2, 1984, Second Session, Thirty-second Parliament, 32-33 Eliz. II, 1983-84. See: S.31.78 for interim injunctions and S.31.91 for interlocutory orders.

> the initial stage.[63] whereas the Competition Act does not.

Because of their almost identical format, the analysis of Bill C-29 shall be deferred to and absorbed into the following discussion pertaining to the current legislation.

The preceding historical overview highlights the issues which will be of concern when investigating the injunctive provisions of the current legislation. The differing proposals over the past decade and more spot the issues which may be of contemporary concern. The appropriate burden of proof on the applicant is of major concern in the Competition Act. The elements of the test for provisional relief themselves are debatable. Whether an application prior to or subsequent to the initiation of formal proceedings is of any relevance must be determined. A related matter must address the compulsory nature of such obligations imposed on the Director. And finally, the constraints placed on the duration and extension of interim orders raise policy questions. As a consequence of studying the recent development of the present enactments, one recognizes that these issues have been promoted to the forefront of policy analysis.

D THE ORDINARY PRINCIPLES GOVERNING PROVISIONAL INJUNCTIONS

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[63] Ibid., S.31.72.

1. INTRODUCTION

It is becoming increasing evident that the practical determination of the permissibility of proposed or consummated mergers will rely often on the prompt and less cumbersome injunctive proceedings. The provisional or temporary injunction is available at the pre-trial stage to temporarily check the further progress of the transaction. Injunctions are usually prohibitive in nature, resembling in many respects a typical restraining order forbidding the respondent from doing a certain act. In the case of a proposed or incomplete merger, a prohibitive injunction could take two forms: the order could act as an absolute bar to any future activity which could further the progress of the merger or it might resemble a "hold separate and apart" order which would prohibit the actual technical completion of the merger while allowing ongoing activity to proceed. A more infrequent form of injunction is the mandatory injunction which is similar in nature to the remedy of specific performance or the prerogative writ of mandamus. The prohibitive injunction will likely be the form most often employed to restrict and prevent undesirable merger activity.

A final injunction is granted when the rights of the parties are determined. In the case of anticompetitive mergers, such permanent injunctions would be granted after the trial of the issue on its merits. In contrast, the important functionality of the provisional or temporary injunction emerges because these orders are granted prior to the final hearing and determination of the matter in issue. The parties are temporarily prevented from inextricably melding an enterprise which would be subsequently difficult, and perhaps impossible, to dismember.

Provisional injunction applications may be made on notice or ex parte. The civil procedure rules will be governed by the rules of the superior courts of the individual provinces and thus may vary in particulars. However, citing as an example the Rules of Court[66] for the province of Alberta, the application for a temporary injunction shall be made by notice ~~of motion~~ and shall be given to all parties affected.[67] The notice of motion shall state the relief sought[68] and be heard by a judge sitting in chambers.[69] The order may be enforced against all persons bound thereby.[70] The rules are ambiguous as to whether an injunction so obtained could be granted and enforced against a person who was not named in the application.[71] Unless leave is granted by the court, two days notice is required to be served on the parties affected.[72] Provisions are available to make an ex parte application if the court is satisfied that no notice is necessary and delay might entail serious mischief.[73] It is imperative to emphasize that, at the hearing, evidence is adduced by way of affidavit and that the deponent may be cross-examined on his affidavit.[74] As the rules governing examinations for discovery apply,[75] facts in the belief, not the knowledge, of the deponent may be elicited[76] concerning matters "touching the question at issue."[77] The evidence need not be known to the witness nor relevant in the strict sense required for admissability at trial. Finally, an injunctive order may be modified, varied or rescinded at the discretion of the court.[78]

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[66] Alta. Reg. 390/68 as am.
[67] Alta. Reg. 313/81, R.384(1).
[68] Ibid., R.384(2).
[69] Ibid., R.385.
[70] Ibid., R.341.

Provisional injunctions are equitable remedies which are at the discretion of the courts to grant. Consequently, the applicant must come to the court with "clean hands" and make a full and frank disclosure of all material facts. The Judicature Act sets out in very broad terms the jurisdiction of the court to grant temporary or provisional injunctions:

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[71] Under S.72(1) Competition Act, an interim order issued by the Tribunal is only enforceable against a person named in the application. Under R.384(1), Alta. Reg. 313/81, all persons who are affected by the notice of motion must be named in the application; consequently, it would appear that the applicant is required to determine prior to the hearing all possible transgressors. It should be noted that under the previous R.357(2), Alta. Reg. 390/68, the order could be enforced against those who were not parties.

[72] Supra, n.67, R.386.

[73] Ibid., R.387(1).

[74] Ibid., R.314(1).

[75] Ibid., R.314(2).

[76] Ibid., R.305(3).

[77] Ibid., R.200(1).

[78] Ibid., R.387(2).

> 13(2) An order in the nature of a mandamus or injunction may be granted or a receiver appointed by an interlocutory order of the Court in all cases in which it appears to the Court to be just or convenient that the order should be made, and the order may be made either unconditionally or on any terms and conditions the Court thinks just.''

The court is under no compulsion to issue an injunction. As further stated in the Judicature Act, the court may award damages, or any other relief it considers just, in lieu of a provisional injunction:

> 20. In all cases in which the Court has jurisdiction to entertain an application
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> (a) for an injunction against
>
> (i) a breach of a covenant, contract or agreement, or
>
> (ii) the commission or continuance of a wrongful act,
> or
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> (b) for the specific performance of a covenant, contract or agreement, the Court if it thinks fit may

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'' Judicature Act, R.S.A. 1980, c.J-1, S.13(2), as am. See the following cases for a discussion of the principle that an injunctive order must be based on an existing substantive right, but may develop novel remedial solutions:
Siskina v. *Distos Compania Naviera S.A.*, [1979] A.C. 210 (H.L.); *Bremer Vulkan Schiffban and Maschinen Fabrik* v. *South India Shipping Co. Ltd.*, [1981] A.C. 909 (H.L.).

> award damages to the injured party either in addition to or in substitution for the injunction or specific performance, and the damages may be ascertained in any manner the Court may direct, or the Court may grant any other relief that it considers just.[11]

2. PRELIMINARY OR QUIA TIMET INJUNCTIONS

Provisional injunctions are further categorized according to whether the damages are real or merely apprehended. For simplicity in the following discussion injunctions which are granted subsequent to the realization of damages shall be referred to as interlocutory, while injunctions which anticipate loss shall be designated as preliminary, quia timet, or injunctions. Note that in general either type of injunction may enjoin proposed mergers and consummated transactions. In most cases, however, the preliminary injunctions will be directed towards proposed, and the interlocutory orders towards perfected mergers. One must be careful not to confuse the interpretation applied to interlocutory injunctions mentioned above with the ordinary meaning applicable in s. 76 Competition Act. Under this section, a proceeding under s. 64 Competition Act must already be in progress in order to avail oneself of this provision. In this sense, a s. 76 interlocutory application can deal with "expected" injury because the substantive provisions in s. 64 Competition Act govern proposed as well as completed mergers. This complexity notwithstanding, the following discussion, for the purposes of clarity, will presuppose that s. 72 will focus on anticipated injuries, while s. 76 will emphasize realized losses.

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[11] Ibid., S.20.

Injunctions quia timet[61] necessitate establishing the propriety of injunctive relief without actual evidence as to the nature of the harm inflicted. The applicant requests relief before he has suffered any demonstrable harm. The jurisdiction of the courts to grant such extraordinary relief is indisputable,[62] but a severe burden of proof is imposed on the party seeking relief. The courts have consistently imposed a burden of proof requiring the applicant to do more than merely "tip the scales". In some cases, a "high probability" of harm was required to be established;[63] other cases required a "great probability"[64] or an "extreme probability".[65] The cautious approach by the courts in granting an injunction quia timet was manifest in this onerous burden of proof; the threatened harm had to be so sufficiently imminent that only by granting the injunction could serious harm to the applicant be avoided.

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[61] Literally, "because he fears".

[62] See: Scott Rural Municipality v. Edwards, [1934] S.C.R. 332, [1934] 3 D.L.R. 793 (Sask.C.A.).

[63] Fletcher v. Bealey (1885), 28 Ch.D. 688.

[64] Pattison v. Gilford (1874), L.R. 18 Eq. 259.

[65] A.G. v. Kingston-on-Thames Corp. (1865), 34 L.J. Ch. 481.

In the frequently cited case, Earl of Ripon v. Hobart,[86] Brougham, L.C., indicated that the issue involves "balancing the magnitude of the evil against the chances of its occurrence." In essence, Lord Brougham was requiring a high probability of substantial harm before entertaining the granting of a preliminary injunction.

Some concerns arise as a result of the development of the jurisprudence respecting quia timet proceedings. First, the degree of burden of proof incumbent on the applicant is relatively high; this will restrict the preventative nature of the remedy and induce the applicant to suffer actual loss before trying the issue on the merits under the familar civil burden of proof. Secondly, the courts are constantly cognizant of the risk of opening the floodgates to litigation. Lastly, the potentially injured party must time his application precisely. If the application is made too early, then the respondent may argue that the proceedings are premature and loss is not sufficiently imminent. Conversely, if the applicant delays in bringing his application before the court, he may be unsuccessful on the grounds that immediate temporary relief is obviously not required and the resolution lies in damages only. In summary, injunctions quia timet may be granted where no damages have been established but the courts will be extremely prudent and reluctant to exercise their equitable discretion.

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[86] Earl of Ripon v. Hobart (1834), 3 My. & K. 169, 40 E.R. 65.

3. INTERLOCUTORY INJUNCTIONS

The term interlocutory has garnered several meanings in the literature and jurisprudence. There is often a definitional distinction made between interlocutory and interim injunctions; an interlocutory injunction usually subsists until the final disposition of the issue, whereas an interim injunction restrains the respondent for a specified time only. This distinction is not material to the merger issue. In contrast to a preliminary injunction which is issued prior to the commencement of an action, an interlocutory order is granted during the progress of ongoing litigation. Finally, an interlocutory injunction may connote an order which has been obtained subsequent to realized loss suffered by the applicant in contrast to being granted prior to actual damages. These final two characteristics of post-application and post-injury will govern the following analysis.

Under the general rubric of interlocutory injunctions, four sub-classifications are discernible:

1. Interlocutory Injunction - an order restraining the respondent until the trial or disposition of the matter,

2. Interim Injunction - a subset of the preceding class, restraining the respondent for a period terminating prior to trial or disposition,

3. Mareva Injunction[87] - the right to seize exigible assets when found within the jurisdiction, wherever the respondent may be, and
4. Anton Piller Injunction[88] - an interlocutory order allowing a search and seizure for the applicant's documents.

The Mareva and Anton Piller injunctions do not appear to have general application to the merger issue; the fundamental inquiry should focus on the principles and doctrines of law governing the granting of order restraining a merger subsequent to the commencement of proceedings alleging real or apprehended injury or damages.

An interlocutory injunction, although usually sought on notice, may be obtained ex parte. Such an ex parte order may be interim for a specified period,[89] or interlocutory in the sense of continuing until final disposition.[90] The test to be applied by the court requires proof that the delay necessary to give adequate notice might entail serious and irreparable injury to the applicant.[91] It must be highlighted that this one-sided standard is only applicable to the issue of dispensation of notice, not the issuance of the order itself. Of utmost importance is the positive duty on the applicant for an *ex parte* order to make complete disclosure of all relevant material and possibly even make further inquiries.[92] As in the case of all provisional injunctive applications, the evidence as to the belief of the matters relating to the issue are adduced in affidavit form and subject to cross-examination.

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[87] Mareva Compania Naviera S.A. v. International Bulkcarriers Ltd., [1975] 2 Lloyd's Rep. 509 (C.A.).

[88] Anton Piller K.G. v. Manufacturing Processes Ltd., [1976] Ch. 55 (C.A.).

[89] Century Engineering Co. Ltd. v. Greto (1960), 26 D.L.R. (2d) 300, [1961] O.R. 85 (H.C.J.)

[90] Canadian Pacific Airlines Ltd. v. Hind (1981), 122 D.L.R. (3d) 498, 32 O.R. (2d) 591 (H.C.J.).

4. THE BASIC TEST FOR PROVISIONAL INJUNCTIONS

(a) General Principles

Historically, the courts had applied a checklist of discretionary factors in an effort to maintain a significant degree of flexibility in determining the availability of provisional injunctions. These factors were not restricted to watertight compartments; they were inherently interdependent and simply allowed the courts to focus their attention on the relevant issues. It was ultimately a matter for the judge to attach the appropriate weight to each element. A review of the jurisprudence before 1975 permits a simplified compilation of four primary factors which the courts considered when contemplating the issuance of a provisional injunction:

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[91] *Gulf Islands Navigation Ltd.* v. *Seafarer's International Union of North America* (1959), 18 D.L.R. (2d) 216 (B.C.S.C.).

[92] *Launch! Research & Development Inc.* v. *Essex Distributing Co.* (1977), 4 C.P.C. 261 (Ont. H.C.J.).

1. Strength of Case - If the applicant had a strong prima facie case, this would increase the likelihood of success for provisional relief;

2. Balance of Risk - This element has been subdivided into two secondary factors as follows:
    (a) Irreparable harm to applicant - the issue here is the degree and probability of damage that would be incurred by the applicant if the order were refused and the applicant were to succeed ultimately at trial;
    (b) Irreparable harm to the respondent - conversely, the courts will weigh the probability and degree of loss to be suffered by the respondent if the injunction were granted and the respondent were to succeed on the merits;

3. Balance of Convenience - This element is very similar to the balance of risk criterion, however emphasis is placed on the net effect. The balance of convenience

lies with the party who is incapable of being compensated by way of damages. Unless the balance of uncompensatory harm is substantial, the courts will tend to preserve the status quo;

4. Special Factors - this element serves as a "basket clause" for all other equitable considerations, including:
   (a) the conduct of the parties;
   (b) alternative remedies;
   (c) delay and prematurity;
   (d) the effectiveness of the order.

Turning first to the question addressing the strength of the plaintiff's case, the courts have always pondered whether or not the plaintiff had a strong prima facie case. Prima facie, in this context, implies circumstances where the court would allow the plaintiff to succeed solely on the material before it, if the court were required to render a final decision. It would appear that four possible outcomes could arise from the application of a prima facie test at the outset of the deliberation:

1. A strong prima facie case, eliminates the need to consider the balance of convenience. This principle has not been accepted by the courts because it ignores the risk of deciding the issue on a preliminary assessment.

2. A strong prima facie case still requires that attention be afforded the remaining three factors.

3. A weak prima facie case does not prohibit the adjudicator from entertaining the remaining three issues. At the preliminary stage, it is often difficult to determine the case on its merits, therefore the court is compelled to consider the risks of damage to the parties and other factors in addition to the possible outcome at trial.[13]
4. A weak prima facie case precludes the judge from the deliberation of the remaining three relevant issues to

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[13] Dwyre v. Ottawa (1898), 25 O.A.R. 121 (Ont.C.A.), at p. 130, per Moss, J.A.: "The rules governing applications of this kind are well settled. Where the legal right is not sufficiently clear to enable the Court to form an opinion it will generally be governed in deciding an application for an interim injunction by considerations of the relative convenience and inconvenience which may result to the parties from granting or withholding the order."

See the following cases where the absence of a prima facie case did not preclude the court from granting interlocutory relief:
Hubbard v. Vosper, [1972] 2 Q.B.84 (C.A.).
Gladstone Petroleums Ltd. v. Husky Oil (Alberta) Ltd. (1969), 9 D.L.R. (3d) 415 (Sask. Q.B.).
Lido Industrial Products Ltd. v. Melnor Manufacturing Ltd., [1968] S.C.R. 769, 69 D.L.R. (2d) 256.
Steel Art Co. Ltd. v. Hrivnak (1979), 105 D.L.R. (3d) 716, 27 O.R. (2d) 136 (H.C.J.).

be considered.[94] This has often been referred to as the "threshold test". It involved:

> [S]equentially, an inquiry as to whether the plaintiff had demonstrated a sufficient probability of right, and, assuming that the threshold test was met, further inquiry as to the adequacy of damages or other relief, and what the relative position of the parties would be if interlocutory relief was not granted.[95]

(b) The Test in American Cyanamid

There are no Canadian or English superior court decisions which decide the availability of provisional injunctions exclusively on the existence of a strong *prima facie* case. A strong *prima facie* case would invariably indicate that the applicant would suffer harm by succeeding at trial, having been denied temporary relief. However, the result of a preliminary inquiry which does not establish a strong *prima facie* case has been the subject of much controversy. The Court of Appeal in *American Cyanamid*[96] applied the strength of the plaintiff's case as a threshold test and therefore ignored the balance of convenience and other special factors. The fact that the plaintiff did not establish a *prima facie* case effectively precluded the court from reviewing the other variables:

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[94] See the following cases for this approach:
Salada Foods Ltd. v. *W.K. Buckley Ltd.* (No. 2) (1973), 9 C.P.R. (2d) 35 (Fed. Ct. T.D.).
Cradle Pictures (Canada) Ltd. v. *Penner* (1975), 63 D.L.R. (3d) 440, 10 O.R. (2d) 444 (H.C.J.).
Bain v. *Bank of Canada and Woodward*, [1935] 4 D.L.R. 112 (B.C.C.A.).

[95] Hammond, "Interlocutory Injunctions: Time for a new Model". (1980) 30 *U. of T. L.J.* 240.

[96] *American Cyanamid Co.* v. *Ethicon Ltd.*, [1974] F.S.R. 312 (C.A.).

> [I]f there be no *prima facie* case on the point essential to entitle the plaintiff to complain of the defendants' proposed activities, that is the end of the claim to interlocutory relief."[97]

The landmark decision of the House of Lords in *American Cyanamid*[98] overturned the decision of the Court of Appeal and granted the injunction. The plaintiff in *American Cyanamid* owned a patent on sterile absorbable surgical sutures. The defendant, Ethicon, controlled the market for "catgut" sutures in the United Kingdom and proceeded to develop a synthetic suture very similar in nature to American Cyanamid's. On application for an injunction *quia timet*, American Cyanamid alleged infringement of its patent. The evidence was extremely complex at trial, taking eight days to complete.[99] The core issue queried whether there existed a rule of law that compelled the court to first determine if a *prima facie* case existed before being able to evaluate the balance of convenience and other factors. As Lord Diplock, L.J., posited:

Nevertheless this authority was treated by Graham J.

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[97] *Ibid*., p. 333, per Russell, L.J.

[98] *American Cyanamid Co.* v. *Ethicon Ltd.*, [1975] A.C. 396 (H.L.); [1974] F.S.R. 312 (C.A.).

[99] This would be similar to complex economic evidence elicited on application for an injunction to enjoin a proposed merger.

> and the Court of Appeal in the instant appeal as leaving intact the supposed rule that the court is not entitled to take any account of the balance of convenience unless it has first been satisfied that if the case went to trial upon no other evidence than is before the court at the hearing of the application the plaintiff would be entitled to judgment for a permanent injunction in the same terms as the interlocutory injunction sought.'[100]

The House of Lords had to address the judgment of the lower Court of Appeal which had established the principle of law:

> They [Court of Appeal] considered that there was a rule of practice so well established as to constitute a rule of law that precluded them from granting any interim injunction unless upon the evidence adduced by both the parties on the hearing of the application the applicant had satisfied the court that on the balance of probabilities the acts of the other party sought to be enjoined would, if committed, violate the applicant's legal rights. In the view of the Court of Appeal the case which the applicant had to prove before any question of balance of convenience arose was "prima facie" only in the sense that the conclusion of law reached by the court upon that evidence might need to be modified at some later date in the light of further evidence either detracting from the probative value of the evidence on which the court had acted or proving additional facts. It was in order to enable the existence of any such rule of law to be considered by your Lordships' House that leave to appeal was granted.'[101]

The object of interlocutory or, for that matter, preliminary relief is to balance the risk of uncompensatory damages to the plaintiff and defendant in the event the outcome at trial differs from the preliminary disposition:

> The object of the interlocutory injunction is to protect the plaintiff against injury by violation of his right for which he could not be adequately

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[100] *Supra*, n.98, p. 407.
[101] *Ibid*., p. 405.

> compensated in damages recoverable in the action if the uncertainty were resolved in his favour at the trial; but the plaintiff's need for such protection must be weighed against the corresponding need of the defendant to be protected against injury resulting from his having been prevented from exercising his own legal rights for which he could not be adequately compensated under the plaintiff's undertaking in damages if the uncertainty were resolved in the defendant's favour at the trial. The court must weigh one need against another and determine where "the balance of convenience" lies.'[102]

If the court were required to find that the plaintiff possessed a strong case before being permitted to weigh the balance of convenience, then the primary issue for provisional relief would not even be considered. The court need not undertake a preliminary trial on the merits to be afforded the opportunity to balance the relevant risk of harm to the parties. Lord Diplock expressly rejects the exclusionary rule of law proposed by the Court of Appeal:

> Your Lordships should in my view take this opportunity of declaring that there is no such rule. The use of such expressions as "a probability," "a prima facie case," or "a strong prima facie case" in the context of the exercise of a discretionary power to grant an interlocutory injunction leads to confusion as to the object sought to be achieved by this form of temporary relief. The court no doubt must be satisfied that the claim is not frivolous or vexatious; in other words, that there is a serious question to be tried.'[103]

His lordship simply requires that the plaintiff have a case to be tried, an action which is not vexatious or frivolous:

> So unless the material available to the court at the hearing of the application for an interlocutory injunction fails to disclose that the plaintiff has any

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[102] *Ibid*., p. 406.
[103] *Ibid*., p. 407.

> real prospect [emphasis added] of succeeding in his claim for a permanent injunction at the trial, the court should go on to consider whether the balance of convenience lies in favour of granting or refusing the interlocutory relief that is sought.'[104]

The judgment proceeds to outline a five step procedure to be followed:

1. There must be a credible dispute;
2. The balance of risk must be assessed;[105]
3. The balance of convenience is elevated to primary importance;[106]
4. The strength of the plaintiff's case is relegated to a subordinate role;[107]
5. Finally, other special factors may be considered.

In placing the judgment in perspective, it must be remembered that a branch of the jurisprudence prior to American Cyanamid did not require proof of a prima facie case in order for the courts to examine the other relevant issues. The House of Lords was primarily burdened with the task of circumventing the exclusionary rule expounded by the Court of Appeal. Moreover, proof of a prima facie case is only a necessary, not sufficient condition for success. A potentially strong case at trial does not guarantee the granting of a provisional injunction; conversely, a predicted weak argument on the merits does not preclude the issuance of an interim order. But this weak case must be enhanced and counterbalanced by a relatively strong and convincing case on the balance of convenience. Due to the fact that the potential for harm to the defendant if the plaintiff does not succeed at trial is inextricably related to the probability of the plaintiff's ultimate success, and because the balance of convenience will be subject to the burden of proof on a balance of probabilities, the net result may certainly be a standard on the applicant which is not significantly different than the usual civil test. If one considers Lord Diplock's concluding remarks on the subject, this deduction is not inconsistent.[104]

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[104] Ibid., p. 407.

[105] Ibid., p. 408.

[106] Ibid., p. 409:
"The extent to which the disadvantages to each party would be incapable of being compensated in damages in the event of his succeeding at the trial is always a significant factor in assessing where the balance of convenience lies."

[107] Ibid., p. 409:
"and if the extent of the uncompensatable disadvantage to each party would not differ widely, it may not be improper to take into account in tipping the balance the relative strength of each party's case as revealed by the affidavit evidence adduced on the hearing of the application. This, however, should be done only where it is apparent upon the facts disclosed by evidence as to which there is no credible dispute that the strength of one is not justified in embarking upon anything resembling a trial of the action upon conflicting affidavits in order to evaluate the strength of either party's case."

Lord Diplock had attenuated the significance of the strength of the plaintiff's case by rejecting the threshold test and had placed greater reliance on the balance of convenience. In order to assess the damages to which the plaintiff, Cyanamid, might well be subjected, Lord Diplock affirmed the "special factors" which were evaluated by Graham, J., at trial.[189] First, the defendant, Ethicon, was not yet in the market; consequently, the defendants would not lose any business nor would employment be affected. Second, Cyanamid would lose its chance of continuing to increase its share of the market until the date of trial. Lastly, it might have been commercially impracticable, due to a marketing backlash, for Cyanamid to deprive the public of Ethicon's absorbable sutures after they had been accepted. In summary, American Cyanamid was decided by balancing the potential risk of harm which would be suffered by the parties and such deliberation was not predicated on the condition precedent that the applicant process a strong probability for success at trial.

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[104] Ibid.

(c) Subsequent Jurisprudence

The judgment of the House of Lords in American Cyanamid has left the state of Canadian jurisprudence in an unsettled position. The principles enunciated in American Cyanamid have been followed in many Canadian cases,[110] however many other decisions which have rejected[111] or merely paid lipservice[112] to it. Steele, J., in his judgment in *Carlton Realty* conjectures:

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[189] Ibid., pp. 409-410.

> The *American Cyanamid* case sets standards that appear in their words to be more lenient than the words '*prima facie* case' or 'probability of success'. I am of the opinion that there is not serious difference. Surely a question to be tried equates to a *prima facie* case.[113]

In many cases, the factors other than those required to assess the strength of the plaintiff's case are indeed irrelevant. Balancing the risk of harm would simply misdirect and divert the court's attention from the true issue governing the appropriateness of provisional relief.

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[110] See:
Yule, Inc. v. *Atlantic Pizza Delight Franchise (1968) Ltd.* (1977, 80 D.L.R. (3d) 725, 17 O.R. (2d) 505 (H.C.J.).
Thomas Lindsay Ltd. v. *Lindsay* (1975), 64 D.L.R. (3d) 761 (B.C.S.C.).
Abouna v. *Foothills Provincial General Hospital Board* (1975), 65 D.L.R. (3d) 337 (Alta. S.C.T.D.).
Re Greenpeace Foundation of British Columbia and Minister of Environment (1981), 122 D.L.R. (3d) 179 (B.C.S.C.).
McFetridge v. *Nova Scotia Barristers' Society* (1981), 122 D.L.R. (3d) 627 (N.S.S.C.).
Steel Art Co. Ltd. v. *Hrivnak* (1979), 105 D.L.R. (3d) 716, 27 O.R. (2d) 136 (H.C.J.).

[111] See:
Cradle Pictures (Canada) Ltd. v. *Penner* (1975), 63 D.L.R. (3d) 440, 10 O.R. (2d) 444 (H.C.J.).
Toronto Marlboro Major Junior "A" Hockey Club v. *Tonelli* (1975), 67 D.L.R. (3d) 214, 11 O.R. (2d) 664 (H.C.J.).
Niagara Frontier Caterers Ltd. v. *Lukey* (1975), 24 C.P.R. (2d) 280 (H.C.J.).
Canadian Javelin Ltd. v. *Sparling* (1978), 4 B.L.R. 153 (Fed. Ct. T.D.).

[112] See: *Heathview Developments Ltd.* v. *Credit Froncier* (1982), 37 O.R. (2d) 262 (H.C.J.).

[113] *Carlton Realty Co. Ltd.* v. *Maple Leaf Mills Ltd.* (1978), 93 D.L.R. (3d) 106, 22 O.R. (2d) 198 (H.C.J.), *per* Steele, J., at p. 203. It is submitted in this case that the court was attempting to equate "a reasonable prospect for success" to the standard requiring that the case not be "frivolous or vexatious".

In Fellowes & Son v. Fisher,[114] the English Court of Appeal concluded, in an action to enforce a non-competition restrictive covenant, that the probability of predicting the interpretation of the contract at trial was reasonably high. Brown, L.J., by arguing in favour of incorporating the strength of the plaintiff's case in the balancing formula, implicitly acknowledges the interrelationship of the two primary issues involved in granting interlocutory relief:

> I confess that I cannot see how the 'balance of convenience' can be fairly or reasonably considered without taking some account as a factor of the relative strength of the parties cases.[115]

Many cases subsequent to American Cyanamid hold that the plaintiff is still required to show a strong prima facie case to obtain an interim injunction to restrain a breach of a restrictive covenant in restraint of trade.[116] In addition to considering the ultimate outcome of the dispute in circumstances where such outcome is readily predictable beforehand, the courts have been inclined to weigh the strength of the case where the preliminary decision will most likely and for all practical purposes decide the issue completely. In N.W.L. Ltd. v. Woods,[117] Lord Diplock himself seems to broaden the principles laid down in American Cyanamid:

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[114] Fellowes & Son v. Fisher, [1976] Q.B. 122 (C.A.).

[115] Ibid., p. 138.

[116] See:
Weight Watchers of Manitoba Ltd. v. Peters (1979), 6 Man. R. (2d) 44 (Q.B.).
Drake Int'l Inc. v. Wortmann (1980), 108 D.L.R. (3d) 133, 27 O.R. (2d) 707. (Div. Ct.).
W.R. Grace & Co. of Canada Ltd. v. Save (1980), 111 D.L.R. (3d) 204, 28 O.R. (2d) 612 (H.C.J.).

> Where, however, the grant or refusal of the interlocutory injunction will have the practical effect of putting an end to the action because the harm that will have been already caused to the losing party by its refusal is complete and of a kind for which money cannot constitute any worthwhile recompense, the degree of likelihood that the plaintiff would have succeeded in establishing his right to an injunction if the action had gone to trial is a factor to be brought into the balance by the judge in weighing the risks that injustice may result from his deciding the application one way rather than the other.[118]

The Manitoba Court of Appeal has rejected the American Cyanamid formulation in favour of an integrated two-part test in the Lambair Ltd.[119] case; the Alberta Court of Appeal has also rejected the application of the rule to covenants in restraint of trade in the Erickson[120] case. In contrast, the Ontario Court of Appeal has provisionally accepted the principle that a strong prima facie case is not a necessary prerequisite to obtaining an interlocutory injunction.[121]

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[117] N.W.L. Ltd. v. Woods, [1979] 1 W.L.R. 1294 (H.L.).

[118] Ibid., p. 1307.

[119] Lambair Ltd. v. Aero Trades (Western) Ltd. (1978), 87 D.L.R. (3d) 500 (Man. C.A.).

[120] Erickson v. Wiggins Adjustments Ltd., [1980] 6 W.W.R. 188 (Alta. C.A.).

Although the Supreme Court of Canada has not addressed the issue in American Cyanamid directly, several recent statements at this level have been included as obiter dicta. In Vignola v. Keable,[122] Beetz, J., incidentally states that, "It is doubtful [emphasis added] that the fears expressed in the motion for an injunction will be realized in the future." Perhaps without consciously envisaging the matter, the court has considered that the strength of the case is not strong. The final outcome on the merits has not been consigned to a subsidiary role. Most recently, the Supreme Court of Canada found an opportunity on application for a Mareva injunction in Aetna Financial Services v. Feigelman[123] to restate the historic principle for interlocutory injunctions by quoting from the decision in Chesapeake v. Ball:

> The granting of an interlocutory injunction is a matter of judicial discretion, but it is a discretion to be exercised on judicial principles. I have dealt with this matter at length because I wish to emphasize how important it is that parties should not be restrained by interlocutory injunctions unless some irreparable injury is likely to accrue to the plaintiff, and the Court should be particularly cautious where there is a serious question as to whether the plaintiff would ever succeed in the action. I may put it in a different way: If on one hand a fair prima facie case is made out and

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[121] Yule, supra, n.110.

[122] Vignola v. Keable, [1983] S.C.C.D. 1894-01, 51 National Reports 143, at p. 158.

[123] Aetna Financial Services Ltd. v. Feigelman, [1985] S.C.C.D. 1895-01.

> there will be irreparable damage if the injunction is not granted, it should be granted, but in deciding whether an interlocutory injunction should be granted the defendant's interests must receive the same consideration as the plaintiff's.[124]

As a result of the case law subsequent the American Cyanamid, both in Canada and the United Kingdom, the principle of law has evolved that a weak strength of case argument will not preclude an analysis by the courts of the risks of harm involved. Furthermore, the consideration to be afforded to strength of case issue will be considerably more than that attributed by Lord Diplock in American Cyanamid. Mr. Justice Estey, speaking for a unanimous court, observes in *obiter dicta*, that no rule of law exists requiring proof of a *prima facie* case as a prerequisite to consider other factors:

> Reconsideration of the requirement that the plaintiff must show a "strong *prima facie* case" has come in the wake of the decision of the House of Lords in America Cyanamid Co. v. Ethicon Ltd., [1975] A.C. 396. However, the other principles enunciated by McRuer C.J.H.C. remain unimpaired. As a general proposition, it can be fairly stated that in the scheme of litigation in this country, orders other than purely procedural ones are difficult to obtain from the Court prior to trial. Where the injunction maintains the status quo in a way which is fair to both sides, the order is attainable; but, simply because the order would not injure the defendant is not sufficient reason to move the Court to grant what is generally regarded as an extraordinary intervention.[125]

The court appears to be endeavoring to preserve maximum flexibility and discretion in issuing extraordinary remedies.

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[124] Chesapeake & Ohio Railway Co. v. Ball, [1953] O.R. 843 (H.C.J.), p. 854-55.

[125] *Supra*, n.123, p. 5.

Although on first blush the principles delineated in American Cyanamid appear to provide for a diminution of the onus of proof respecting the merits of the case, it is submitted that the jurisprudence viewed in its entirety establishes a more resilient and flexible two-part standard. The strength of the plaintiff's case *and* the balance of convenience are combined impartially and then weighed according to the particular circumstances of the case. As Rogers and Hately observe:

> The breadth of potential application of Lord Diplock's amended version of American Cyanamid has yet to be established, but it clearly offers a route for returning to the former reliance on the test of a strong *prima facie* case where the courts most want and need it.[126]

Although a weak preliminary case will more than likely greatly diminish the potential for a successful application, it will not by the same token singly deny a successful application. Rogers and Hately offer, as a practical guide, the suggestion that:

> Whether or not the *American Cyanamid* test is applied, a strong legal case cannot but help persuade the court that an injunction is deserved.[127]

The most succinct summary emphasizing the intermixture of the pertinent concepts may be found in the judgment of

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[126] B.M. Rogers and G.W. Hately, "Getting the Pre-Trial Injunction". (1982) 60 *Canadian Bar Rev.* 1, at p. 17

[127] *Ibid*., pp. 14-15.

Steele J. in Yule Inc., where in his Lordship states:

> The cases often refer to a prima facie case, a fair prima facie case, a strong prima facie case, not a frivolous or vexatious case, a chance of success, a probability of success, a serious question to be tried, a substantial issue to be tried. These are only some of the many phrases that have been used in dealing with this matter. While there are differences in degree in all of these phrases, I do not consider them to be substantially different. Each case must be considered on its own merits and then the discretion of the Court must be exercised...The degree to which a Judge will consider the importance of the nature of the case in coming to his conclusion must be weighed with the knowledge of the other factors which he must consider, such as the question of harm to the parties and damages as an alternative, the balance of convenience to the parties and the need, if any, to maintain the status quo.[128]

In an effort to synthesize the salient features of the case law into a general workable framework, it is proposed that the following issues should be considered. First, is an assessment on the merits possible? The response to this query will determine which of two major courses of inquiry should be pursued. If the answer is in the negative, then the adjudicator will be compelled to proceed to evaluate the matter— on the balance of convenience. The fundamental issue at this second stage is to determine where the risk of significant uncompensative harm lies. In a private action suit, this question can be reduced to deliberation on whether the plaintiff could adequately compensate the defendant if the injunction were granted and the plaintiff were unsuccessful at trial. If the balance of convenience lies with the plaintiff, then the injunction should be granted; if it does not, then the order should in most cases be denied. It must be emphasized that an important distinction exists between a difficult and impossible decision. In the case of proposed mergers, the complex and mercurial nature of the circumstances might render the evaluation extremely difficult at a preliminary stage; however this impediment must be weighed against the inability of the state to compensate the parties to the merger in cases where an injunction is issued and the Crown is not able to prove its case at trial.

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[128] Yule Inc., supra, n.110, at pp. 202-203.

In summation, if the plaintiff can satisfy the court on the evidence presently available that the plaintiff will probably succeed at trial, then less weight should be attributed to the balance of risk and other special factors and the issuance of the injunctive remedy seriously considered. On the other hand, if the applicant cannot convince the adjudicator that his action will likely succeed at trial, the court has no option but to consider the relative risks of harm to the parties. It is suggested, however, that a weak prima facie case, one which does not establish that the Crown would suffer irreparable harm without the injunctive protection, would seldom justify the need for extraordinary pre-trial restrictions on the rights of the parties to proceed with the merger.

(d) The Issue of Irreparable Harm

The issuance of a provisional injunction is contingent upon the party who is unsuccessful at the preliminary stage being adequately compensated in damages if the ultimate disposition on the merits rests in its favour. If damages can adequately remedy the harm, then the courts will not entertain an application for an injunction. The financial inability of one party ultimately to be capable of paying damages is a major factor which will predispose the courts in favour of an order. It is only under circumstances where the eventually successful party cannot be adequately recompensed, that "irreparable harm" or "uncompensatory damages" give rise to the need for temporary relief by way of injunction.

Additional difficulties arise in calculating irreparable harm to the applicant when the public interest is at stake. This issue becomes paramount in applications to enjoin mergers because the applicant is applying to enforce the public's right to effective competition, allocative efficiency and competitive prices and products.[123] The merger may not be harmful; determination of this issue requires a reversion to the strength of case problem. Even if the merger is determined to be a net disadvantage to competition, how does one compensate the public at large if the application is denied and the Crown is ultimately successful on the merits.

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[123] See: Competition Act, infra, S.1.1.

In several instances the courts have attempted to broaden the test to include uncompensative harm which would accrue to persons other than the actual applicant.[130] In Smith v. Inner London Education Authority[131] Brown L.J. expresses the view that the interests of the public as a whole should be considered:

> The question of balance of convenience therefore does not arise. Megarry V.C. came to the 'clear conclusion that the balance of convenience favours the grant of the injunctions claimed and not their refusal'. He only considered the balance of convenience as between the plaintiffs and the authority, but I think counsel for the authority is right in saying that where the defendant is a public authority performing duties to the public one must look at the balance of convenience more widely, and take into account the interests of the public in general to whom these duties are owed. I think this is an example of the 'special factors' affecting the balance of convenience which are referred to by Lord Diplock in American Cyanamid Co. v. Ethicon Ltd.[132]

In an application by the British Broadcasting Corporation to enjoin a union from interfering with the international transmission of a World Cup soccer match, Lord Denning in BBC v. Hearn[133] subordinated individual rights to the public interest:

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[130] See: Beaverbrook Newspapers Ltd. v. Keys, [1978] 1 C.R. 582 (C.A.).

[131] Smith v. Inner London Education Authority, [1978] 1 All E.R. 411 (C.A.).

[132] Ibid., p. 422.

[133] BBC v. Hearn, [1978] 1 All E.R. 111 (C.A.).

> I have no doubt whatever that the balance of convenience here is that this Cup Final, in which the whole world is interested, should be transmitted to the Indian Ocean satellite and thence to these many countries. It should not be interfered with by the officers of the union.[134]

Further, in A.G. Ont. v. Yeotes,[135] Labrosse J. extends the scope of irreparable harm which might support the granting of an injunction:

> In line with that decision it is clear, in my opinion, that if a subdivision can be effected by circumventing the Planning Act, irreparable damage to the public interest can be caused which cannot be compensated for in damages.[136]

Even the possibility that the conduct of the respondent might interfere with international trade has strengthened the applicant's case:

> Instead, the relevance of the bridge situation is this. If I am right in refusing this application because no irreparable damages have been shown, the same result should obtain in the case of the bridge. If there is picketing at both the bridge and the tunnel, there will be a most serious interference with international trade across the river, and with the operation of the interrelated industries located in Ontario and Michigan. Applying the test suggested by Cory J. in Yule Inc. v. Atlantic Pizza Delight Franchise (1968) Ltd. et al., it would not be just in the circumstances, in my judgment, that the plaintiff should be confined to a remedy in damages.[137]

The foregoing judgments tend to illustrate that the Crown may possess the right to apply for a provisional injunction on the grounds that, otherwise, the public interest would be detrimentally affected.

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[134] Ibid., p. 118.

[135] A.G. Ontario v. Yeotes (1979), 93 D.L.R. (3d) 332, 111 D.L.R. (3d) 488 (H.C.J.).

[136] Ibid., p. 334.

[137] Detroit & Windsor Subway Co. v. Blyth (1980), 116 D.L.R. (3d) 708, 30 O.R. (2d) 216 (H.C.J.), per Southey, J., at p. 715.

(e) Indemnification

It has been well established that the applicant must provide an undertaking to indemnify the respondent in a situation where an interim injunction is granted.[138] In the event the plaintiff is not successful at trial, the defendant would seek an order for inquiry into damages flowing directly from the injunction. In the Hoffmann-LaRoche[139] case, the Crown, on application to obtain an injunction restraining Hoffmann-LaRoche from charging prices above legal price-ceilings, refused to give an undertaking to indemnify the respondent in the event the ultimate disposition rested not in the Crown's favour. Lord Reid established the general rule that the Crown was obliged to undertake to compensate:

> The respondent's first answer is that when an interim injunction is granted to the Crown no undertaking can be required as a condition of granting it. It is not in doubt that in an ordinary litigation the general rule has long been that no interim injunction likely to cause loss to a party will be granted unless the party seeking the injunction undertakes to make good that

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[138] Vieweger Construction Co. Ltd. v. Rush & Thompkins Construction Ltd., [1965] S.C.R. 195, 48 D.L.R. (2d) 509; Griffin Steel Foundries Ltd. v. Canadian Association of Industrial Mechanical & Allied Workers (1977), 80 D.L.R. (3d) 634 (Man. C.A.).

[139] F. Hoffmann-LaRoche & Co. and A.G. v. Secretary of State for Trade and Industry, [1975] A.C. 295 (H.L.).

> loss if in the end it appears that the injunction was unwarranted. He cannot be compelled to give an undertaking but if he will not give it he will not get the injunction.
> But there is much authority to show that the Crown was in a different position. In general no undertaking was required of it. But whatever justification there may have been for that before 1947 I agree with your Lordships that the old rule or practice cannot be justified since the passing of the Crown Proceedings Act of that year.'[140]

However, where the Crown was endeavoring to enforce the laws of the land, not its own proprietary rights, an exception to the general principle existed:

> So if this had been a case where the Crown were asserting a proprietary right I would hold that the ordinary rule should apply and there should be no interlocutory injunction unless the Crown chose to give the usual undertaking.
> But this is a case in a different and novel field. No doubt it was thought that criminal penalties were inappropriate as a means of enforcing orders of this kind, and the only method of enforcement is by injunction. Dealing with alleged breaches of the law is a function of the Crown (or of a department of the executive) entirely different in character from its function in protecting its proprietary right. It has more resemblance to the function of prosecuting those who are alleged to have committed an offence. A person who is prosecuted and found not guilty may have suffered serious loss by reason of the prosecution but in general he has no legal claim against the prosecutor. In the absence of special circumstances I see no reason why the Crown in seeking to enforce orders of this kind should have to incur legal liability to the person alleged to be in breach of the order.'[141]

The onus was thus shifted to the respondent to show good reason why the state should undertake to compensate:

> But I think that it is for the person against whom the

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[140] *Ibid*., p. 341.
[141] *Ibid*.

interim injunction is sought to show special reason why justice requires that the injunction should not be granted or should only be granted on terms.'[142]

A lenient interpretation of the Hoffmann-LaRoche judgment would justify an application by the Attorney-General to enjoin proposed mergers in the public interest and discard the requirement that the state indemnify the respondent for possible damages. Referring to similar principles, Montgomery, J., in A.-G. Ontario v. Harry[143] did not require the Crown to pay damages, even after undertaking to do so, because the Attorney-General had an arguable case, the respondent had only succeeded on a technicality, and "[t]hese actions were brought by the Attorney-General for the protection of the public and the prevention of public injury [emphasis added]".[144]

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[142] Ibid.

[143] A.-G. Ontario v. Harry (1982), 132 D.L.R. (3d) 73, 35 O.R. (2d) 248 (H.C.J.).

[144] Ibid., p. 76. Note: In Hoffmann-LaRoche, L. Diplock interpreted s.21(1) Crown Proceedings Act, 1947, not to require the Crown to undertake to indemnify if it were protecting the public interest. Section 21(1) of the Act states:

> "In any civil proceedings by or against the Crown the court shall, subject to the provisions of this Act, have power to make all such orders as it has power to make in proceedings between subjects, and otherwise to give such appropriate relief as the case may require:..."

However, L. Diplock, at p. 365, concluded that "in certain circumstances" where the Crown "had a substantial interest in enforcing the order", no undertaking would be required. In Canada, under the Crown Liability Act, R.S.C. 1970, C.C-38, as am., no equivalent provision exists.

A more conservative view of the ratio decidendi in Hoffmann-LaRoche would distinguish the peculiar circumstances in that case from the general merger situation. Lord Diplock outlined the critical issues in Hoffmann-LaRoche as follows:

> In the instant case, the circumstances which, to my mind, are crucial to the exercise of the discretion whether to grant an interim injunction to the Crown without requiring an undertaking as to damages are: first, that the law which the Crown is seeking to enforce by the only means available under the governing statute is an order made by statutory instrument which has been approved by affirmative resolution of each House of Parliament and is valid on its face; secondly, that the appellants threaten to act in a way which they admit would contravene the terms of this order and claim to be entitled to do so upon the ground that the order itself is ultra vires (a) because of unfair conduct by the Monopolies Commission in the course of the investigations which led to their report on which the order was based, and (b) because of the inclusion in that report of recommendations (which the Minister adopted in the order) for the purpose of remedying a mischief to which they were not entitled to have regard; and thirdly, that the Crown itself through the Department of Health and Social Security had a substantial financial interest in enforcing the order.[143]

If one were to apply the foregoing criteria to the merger provisions in either the former Combines Investigation Act or the new Competition Act, first other means are available to enforce the objectives of the legislation. Secondly, the parties to the merger would most certainly deny that their behaviour contravenes the substantive provisions. Lastly, the Crown would seldom have a vested financial interest in enjoining the merger. In summary, while a requirement that the Crown indemnify the parties to a proposed merger would render the injunctive provisions impractical, it is not at all certain that the state of the current jurisprudence would provide an absolute exemption to undertake compensation for damages. Most importantly, such an exclusion would certainly require greater emphasis be placed on determining, at the preliminary stage, the strength of the applicant's case, a result which the balance of risk analysis intended to avoid.

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[143] Supra, n.139, at pp. 364-5.

E INJUNCTIONS UNDER THE COMPETITION ACT

1. INTRODUCTION

The injunctive relief available in the Competition Act[146] has been distilled from the various proposals which have evolved since the Economic Council's Interim Report. In addition, the new provisions have been tailored to facilitate the novel and extensive pre-notification provisions. The provisional or temporary injunctive procedures have been bifurcated into what has been labelled above as a preliminary injunction application and an interlocutory injunction. The preliminary injunction is only available in the instance of a proposed merger.[147] Furthermore, the mechanism for obtaining such preliminary relief may only be invoked under two specific circumstances: First, the Director is precluded from having made an application under the substantive test section. In addition, no previous application may have been made for preliminary relief under the same section.[148] This element of the preliminary injunction provisions providing availability only prior to an application for disposition on the merits emphasizes the uniqueness of the new provisions. The companion interlocutory injunction provisions are only available subsequent to an application for an order under Part VII.[149] These latter interlocutory provisions are neither merger specific nor generally applicable to prolong the pre-notification "waiting period".

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[146] Competition Act, S.C. 1986, proclaimed 19 June, 1986. This Act was previously Bill C-91, cited as: Bill C-91, "An Act to Establish the Competition Tribunal and to Amend the Combines Investigation Act and the Bank Act and other Acts in consequence thereof", First Reading: December 17, 1985, Passed by the House of Commons, June 5, 1986, Royal Assent: June 17, 1986. First Session, Thirty-third Parliament, 33-34 Eliz. II, 1984-85-86. See: Appendix D for a flowchart of Injunction Relief.

2 PRELIMINARY INJUNCTIONS

(a) Procedure

The purpose of the "pre-application" injunctive relief is intended to be twofold. In general, the provisions are available to the Director to temporarily postpone any proposed merger, whether or not the transaction is notifiable pursuant to section 86 Competition Act. However, more importantly the Director may also utilize the procedure to extend the "waiting period" required for proposed mergers which are obliged to notify and inform under section 95 of the new Act.

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[147] _Ibid_., S.72(1).

[148] _Ibid_.; See: section 64 for the substantive test respecting mergers that competition may not be lessened substantially. S.72(1) sets out these two conditions precedent to the availability of preliminary relief.

[149] Competition Act, S.76.

In the case of proposed mergers, a nimble and efficient method of temporarily holding the transaction in abeyance with minimal harm to all parties is desirable while the Director is afforded breathing room to accumulate information and formulate his position regarding possible prohibitory proceedings. It should be emphasized that the Director is not restricted to apply for the preliminary injunction only in cases where the merger is a notifiable transaction. That is to say, whenever the Director suspects that any proposed transaction may run afoul of the merger provisions, he may make application for a preliminary injunction.

Because of the obvious overlap with the interlocutory provisions, it is not at all apparent why the preliminary injunctions are not restricted to notifiable transactions. It is recommended that preliminary relief be incorporated in Part VIII (Notifiable Transactions) in an effort to unify the pre-merger provisions and clarify the objectives of these injunctions. In order to mitigate the inevitable hardship (on the acquiring firm) caused by the delay, the provisions expressly restrict the duration of the order to a relatively short period.

Under the pre-notification provisions, once notice of a proposed merger has been given to the Director, an automatic "waiting period" is statutorily imposed which requires the parties to hold the companies at least separate and apart for a brief period of time. Following the expiration of this "waiting period" the transaction may proceed irrespective of whether or not the Director has instituted formal proceedings. It is assumed that the preliminary injunction proceedings would be available to the Director in a situation where he has not made application pursuant to section 64 of the bill but required an extension to compile further information and analyze his posture. This specialized extension provision would only be available for "pre-application" situations on a one time basis. If application by the Director has been made under section 64 or a previous application has been made for a preliminary injunction, the alternate interlocutory injunction route must be followed.[158] The effect of such an extension if the preliminary injunction were granted would be to protract the "waiting period" to seventeen (ex parte) or twenty-eight (on notice) days in the case of the short-form filing, or thirty-one (ex parte) or forty-two (on notice) days in the case of the long form filing. Any of these periods could be further extended by successfully applying for an interlocutory injunction[151] in conjunction with commencing formal proceedings under section 64.[152] In brief, the primary intention of the distinctive preliminary injunction provisions is to provide the Director with a vehicle to persuade the Competition Tribunal to grant a single extension to the pre-notification "waiting period."

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[158] Ibid., S.72(1).

Turning firstly to a more detailed examination of the preliminary injunction provisions, the presumably self-contained civil procedure is contained in section 72 of the Act as follows:

> 72.(1) Where, on application by the Director, the Tribunal finds, in respect of a proposed merger in respect of which an application has not been made under section 64 or previously under this section, that
>
> > (a) the proposed merger is reasonably likely to prevent or lessen competition substantially and, in the opinion of the Tribunal, in the absence of an interim order a party to the proposed merger or any other person is likely to take an action that would substantially impair the ability of the Tribunal to remedy the effect of the proposed merger on competition under section 64 because that action would be

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[151] Ibid., S.76(1).

[152] A reasonable interpretation of section 76(1) of the Competition Act would preclude an application for an interlocutory injunction unless an application for an order under Part VII has been made, other than an application for a preliminary injunction.

difficult to reverse, or
(b) there has been a failure to comply with section 86 in respect of the proposed merger,

the Tribunal may issue an interim order forbidding any person named in the application from doing any act or thing that it appears to the Tribunal may constitute or be directed toward the completion or implementation of the proposed merger.

(2) Subject to subsection (3), at least forty-eight hours notice of an application for an interim order under subsection (1) shall be given by or on behalf of the Director to each person against whom the order is sought.

(3) Where the Tribunal is satisfied, in respect of an application made under subsection (1), that
(a) subsection (2) cannot reasonably be complied with, or
(b) the urgency of the situation is such that service of notice in accordance with subsection (2) would not be in the public interest,

it may proceed with the application ex parte.

(4) An interim order issued under subsection (1)
(a) shall be on such terms as the Tribunal considers necessary and sufficient to meet the circumstances of the case; and
(b) subject to subsection (5), shall have effect for such period of time as is specified therein.

(5) An interim order issued under subsection (1) in respect of a proposed merger shall cease to have effect
(a) in the case of an interim order issued on ex parte application, no later than ten days, or
(b) in any other case, no later than twenty-one days,

after the interim order comes into effect or, in the circumstances referred to in paragraph (1)(b), after section 86 is complied with.

(6) Where an interim order is issued under paragraph (1)(a), the Director shall proceed as expeditiously as possible to commence and complete proceedings under section 64 in respect of the proposed merger.

As outlined above, the preliminary injunctive relief is available only if all three of the following conditions are satisfied:[153]

1. There exists a proposed merger,
2. There has been no application made under section 64, and
3. There has been no application previously made under section 72.

If at least one of these conditions is unsatisfied, the Director must resort to an application before the Competition Tribunal for an interlocutory injunction pursuant to the ordinary principles of law governing injunctive relief.

Analogous to the former Combines Investigation Act, notice must be served on each party at least forty-eight hours prior to the application.[154] The two exceptions allowing dispensation of this general notice requirement, which were similarly available in the Combines Investigation Act have been transported into the Competition Act, namely:

1. The forty-eight hour notice period cannot reasonably be complied with,[155] and
2. The matter is of such urgency that it would be in the public interest to dispense with

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[153] Ibid., S.72(1).
[154] Ibid., S. 72(2).
[155] Ibid., S.72(3)(a).

notice.[156]

The difficulties that may arise in retaining the latter provision have been discussed above (Chapter VII B); the primary concern centres around the redundancy of the latter exemption when the former is also available. Notwithstanding this difficulty, the basic format of the notice provisions advances two alternate modes of proceeding, ex parte or on notice.

After the parties have been served, or service has been dispensed with, the Crown must satisfy the Competition Tribunal according to a two-part test.[157] First, the proposed merger must be shown to be reasonably likely to lessen competition substantially. Secondly, the Crown must prove that in the absence of the order, any person is likely to take an action which would substantially impair the Tribunal from remedying the effect on competition by way of a subsequent order, pursuant to section 64, by attempting to reverse the original offending action. In other words, the relief would be available if someone were likely to take an action which would be difficult to subsequently reverse under section 64; however not all difficult to reverse actions would give rise to grounds for a preliminary injunction. That specific action would have to substantially impair the Tribunal from remedying the effect of the proposed merger on competition under section 64 "because that action would be difficult to reverse". (Emphasis added). If both of these criteria were found by the Tribunal to be satisfied, the Competition Tribunal might grant a preliminary injunction forbidding any person named in the application from doing any act to further the merger. On the other hand, if either of the two preceding criteria were successfully negated by the respondents, no preliminary injunctive relief would be available.

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[156] Ibid., S.72(3)(b).

[157] This assumes that there has been no previous non-compliance with the notification provisions under section 86. If there has been, the Crown need only satisfy the Tribunal of the failure to comply. See: S.72(1)(b). Otherwise, the fundamental two-part test to determine the availability of the preliminary injunction is contained in S.72(1)(a).

If the Director satisfies the Tribunal that the elements of the test have been sustained, the Tribunal may, at its discretion, issue an interim order forbidding any person named in the application from taking any action to further the proposed merger.[158] The maximum duration of the order will depend upon whether the application is brought ex parte or on notice. If the application is made ex parte, the interim order will subsist for no longer than ten days after the order is in effect;[159] if the application is made on notice then the order will have effect for no longer than twenty-one days.[140] In the case of non-compliance with the requirements under section 86 to notify and inform the Director of a notifiable transaction, the order will stand from the time the order is in effect until twenty-one days (ten days in the case of an *ex parte* application) after the parties have complied with the applicable pre-notification provisions.[141] Once the interim order has been granted, the Director is under a positive duty to proceed as expeditiously as possible to commence and complete proceedings under section 64.[142] Finally, an appeal lies to the Federal Court of Appeal as if it were a judgment of the Federal Court-Trial Division.[143] An appeal on a matter of fact lies also, with leave, to the Federal Court of Appeal.[144]

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[158] Ibid., S.72(1).
[159] Ibid., S.72(5)(a).

(b) Comparison of S.72 Competition Act and S.29.1 Combines Investigation Act

In comparing S.29.1 Combines Investigation Act and the preliminary injunction provisions of the new Act, the most striking changes have been to tailor the new provisions to accommodate for the pre-notification provisions as well as emphasize the perceived distinction between pre- and post-application relief.- The availability of two separate procedures for provisional injunctive relief, preliminary and interlocutory, is undoubtedly an innovative alteration to the previous legislation.

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[140] *Ibid.*, S.72(5)(b).

[141] *Ibid.*, S.72(5). Mr. Mel Capp, Assistant Deputy Director, has indicated that it was the intention of the Department to allow the injunction to exist *only* up to the time of compliance. The actual wording of the section may not be so construed.

[142] *Ibid.*, S.72(6).

[143] Competition Tribunal Act, S.13(1).

[144] *Ibid.*, S.13(2). Note that this section was added after Second Reading as a result of several committee members concerns that an automatic right for a trial *de novo* existed under the Federal Court Rules.

The underlying concept has not been altered substantially. The Crown, on notice, must convince the adjudicative body that an undesirable merger may be difficult to disentangle unless the interim injunction is granted. Depending upon whether the application is made ex parte or on motion, the interim order is in effect for only a very short and defined time period. Both the Combines Investigation Act and the Competition Act employ identical notice provisions. However, from this juncture onwards, the detailed provisions differ markedly in their policy basis. For ease of recognition and simplicity, a list of the major distinctions between the two remedies is outlined below:

Table I

Comparison of S. 72 Competition Act and S. 29.1 Combines Investigation Act

MATTER	S.29.1 C.I.A.	S.72 COMPETITION ACT
1. Adjudicative Body	1. Court	1. Competition Tribunal
2. Applicant	2. Attorney-General	2. Director

3. Respondent	3. Party to Merger	3. Any Person
4. Type of Merger	4. Proposed or Actual	4. Proposed
5. Merger Specific?	5. No	5. Yes
6. Application under substantive provisions	6. optional	6. Can not have been made
7. Burden	7. "likely"	7. "reasonably unlikely"
8. Effect on Competition	8. Cannot be remedied otherwise	8. lessen competition substantially
9. Additional Elements of Test	9. OR, person to suffer out-weighing and uncompensatable damage	9. irreversible action
10.Non-compliance	10. With S.46.1	10. With S.86
11.Notice	11. 48 hours	11. 48 hours
12.Dispensation	12. (a) not reasonable (b) urgent	12. (a) not reasonable (b) urgent
13.Duration of Order	13. (a) ex parte - 10 days (b) on notice - definite	13. (a) ex parte - 10 days (b) on notice - 21 days
14.Extensions	14. Available	14. Not Available
15.Duty of Director	15. to proceed to commence	15. to proceed to commence
16.Punishment	16. 2 years/fine	16. new s.46.1

As a consequence of not applying exclusively to proposed mergers in the context of pre-notification provisions, S.29.1 Combines Investigation Act tended to simply impose a codified version of the general common law principles for provisional injunctions onto the courts. The common law jurisprudence requires notice of the application, makes provisions for dispensation and allows for extensions and variance of the order. The strength of the plaintiff's case appears to have been codified in S.29.1(a); the balance of convenience standard is very similar to the provisions found in S.29.1(b). The duration of the order was in the discretion of the court. An obvious departure in s. 29.1 from the common law was the obligation of the applicant, in this case the Attorney General, to indemnify the respondent for damages which may have arisen if the injunction were to be granted and the respondent successful at trial. Fundamentally, it was this reliance on the ordinary principles for injunctive relief which distinguish the former Act from the provisions of S.72 Competition Act.

(c) Comparison of S.72 and S.64 Competition Act

It is helpful to compare and contrast the test required in the preliminary injunctive provisions of the Competition Act with that set forth in the substantive provisions. On first glance, it would seem that both procedures apply the same test for proposed mergers, that of the likelihood of preventing or lessening competition substantially. However, it would appear that the burden of proof is less onerous in the injunctive provisions. It is presumed that the phrase 'reasonably likely" was employed to connote a burden of proof which would fall short of the more commonly accepted and understood term "likely" which is present in the substantive provisions. Perhaps this was even a resurrection of the prima facie presumption found in Bill C-42. Moreover, the obvious omission of any express exemptions for counterbalancing economic efficiencies,[165] failing companies[166] or the like would lead one to infer that the intent of the provisions was to provide a greater opportunity to obtain a temporary injunction than a more permanent order under section 64. Some concern should be voiced that the Tribunal may in practice interpret the phrase "reasonably likely" no differently than to require the usual preponderance of evidence. In addition, the exemptions which are available in a section 64 application on the merits may be vicariously transplanted into the preliminary injunction provisions as a result of the reference made (in section 72) to the substantive provisions. Besides, the onus of proving an irreversible action is not a "reasonable likelihood", but merely on the balance of probabilities; thus, the possibility of the applicant succeeding on application for a preliminary order may be effectively reduced. It is submitted that the final objective of a preliminary injunctive provision should be to reduce the evidentiary burden on the applicant. It would be counterproductive to impose on temporary relief provisions a degree of proof which would be equal to or greater than that required for the more detailed and permanent determination of the merits.

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[165] Competition Act, S.68.

[166] Ibid., S. 65(b); The failing company defence was chosen simply to illustrate that none of the exemptions included in section 65 have been included in section 72.

(d) Potential Problems with S.72 Competition Act

In addition to the difficulty discussed above respecting the burden of proof which is most likely intended for S.72 Competition Act, the second element of the test which must be satisfied permits several rather ambiguous interpretations. First, the section is unclear as to whether the Tribunal must be able to remedy the effect of the proposed merger on competition by being easily able to reverse the specific contemplated action or by otherwise issuing an order pursuant to subsection 64(1)(f) to remedy the resultant state of competition remaining. If the former interpretation is intended, then it appears remote that any action which would substantially impair the Tribunal's ability to rectify the effect on competition would not also be difficult to reverse. Conversely, a difficult to reverse action would, most assuredly, substantially impair the Tribunal's ability to remedy the effect on competition. The mere fact that the action is difficult to reverse would exacerbate the Tribunal's capacity to order the merger not to proceed or to proceed under certain specified conditions. The fundamental issue is whether the Tribunal finds that the proposed merger may likely prevent or lessen competition substantially. The process can in fact be halted at any stage of the merging process. One must ponder the interpretation to be given to the phrase "difficult to reverse". Does such phraseology connote actual problems in stopping the legal transaction or do the words imply a broader concept of harm to shareholders, employees and others, or possibly harm to competition itself? If the latter position is accepted, the paramount concern centres around the ability of the Tribunal to ultimately remedy the effect of the proposed action on competition. It is only an incidental issue whether or not the original action can be readily reversed. However, the question of whether or not the Tribunal can ultimately remedy the effect of the action on competition is extremely hypothetical and enters the realm of determining the matter on its merits.

It appears that two reasonable alternate approaches could emerge from judicial interpretation of paragraph 72(1)(a). If the courts emphasize that the objective of the preliminary injunction test is to prohibit actions which are likely to substantially impair the ability of the Tribunal to remedy the anticompetitive effect under section 64, then the fact that the particular action is difficult to reverse is, for all practical purposes, immaterial. The test would envision situations where the parties intend to dismember the acquired firm, sell off the assets or terminate the employment of the directors or senior management. The initial transaction of simply purchasing the shares of the target firm, without more, it is presumed would not be sufficient to satisfy this standard. Consequently, it is not apparent why the phrase, "because that action would be difficult to reverse," is required as an afterthought.

An equally valid construction of the paragraph 72(1)(a) would emphasize the irreversible nature of the action. It is certainly possible to conceptualize a commercial take-over by way of assets or shares which would be extremely difficult to reverse. For example, a divestiture order might be incapable of restoring the status quo in a situation where the vendors had disbursed the proceeds of sale to an innocent third party. It is recommended that the legislation not prejudge what level of severity is required to constitute an irreversible action which would prevent the maintenance of a competitive market. The principal query, which should avoid this factual determination, must assuredly be whether the proposed action should be enjoined because it would likely prejudice the Tribunal in its efforts to reverse the action, not because it would likely impair the Tribunal's efforts to restore the level of competition which existed before the proposed merger was commenced.

In order to reconcile the ambiguities, it is submitted that the second part of the test should be modified to require proof that any party to the merger or the application is likely to take any action which would be difficult to reverse and which would further the merger. The anticompetitive nature of the proposed merger has already been established as a result of the first arm of the test in paragraph 72(1)(a).

If the Director were to satisfy the Tribunal that the proposed merger is reasonably likely to lessen competition substantially, an injunction might still be denied if the Tribunal has the ability, "should the merger or part thereof be completed"[167] to impose constraints ensuring future competitive levels. Since the order under section 64 may only be granted against a party to the proposed merger, the legislation must contemplate a permanent order holding the management, directors, assets or, in the case of newspapers, the editorial staff, separate and apart. This mechanism is similar in principle to the undertakings given by the board of directors of Imasco not to interfere with the business autonomy and integrity of Canada Trust in Imasco's take-over bid of Genstar/Canada Trust. To rely on the immutability and integrety of such undertakings and to ignore the inevitable inducement of a parent corporation to intermingle the operations of its affiliates, public policy must undertake an act of faith. As well, purpose of the entire section must not be lost. The primary rationale for its inclusion is to extend the pre-notification "waiting period". If the preliminary injunction is denied because the Tribunal will not be impaired in ultimately rectifying the effect on competition, the Director will be restrained from extending the period within which the merger must not be completed while investigation and analysis continues. One must not lose sight of the fact that the interim order, if granted, may be in force for no longer than twenty-one days as a temporary measure to avoid future difficulties in dismantling the merger. The preliminary injunction should provide ex ante relief to obviate the potential anticompetitive effects and the corresponding test should reflect this objective; the interim order should not be denied because exogenous restrictions may be imposed on the parties to guarantee compliance after the merger is consummated. In summary, the question of anticompetitive effect should not be a further element circumscribing the "irreversible action"; rather, the likely effect on competition should be addressed when determining whether the proposed merger itself is likely to be offending.

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[167] Competition Act, S.64(1)(f).

The second major concern with S.72 Competition Act focuses on the authority vested in the Competition Tribunal to issue preliminary injunctions. The entire section is invoked by an action which, if executed, would be difficult to reverse. But the relief which would be available would allow the Tribunal to forbid any act which may constitute or be directed toward the furtherance of the merger, not exclusively the action itself which gives rise to the original application. If the action is a necessary link in the procedural chain to complete or effect the merger, then enjoining this action would effectively forestall the merger's progress until an application on the merits pursuant to section 64 might be commenced. Furthermore, it is noteworthy that the Tribunal is not empowered to direct that the merger not proceed; it is merely authorized to forbid "any act or thing" directed toward the furtherance of the merger. However, it is subject to judicial interpretation whether "any act" will include the concept of all possible things which lead to progress of the merger, or whether the section will be "read down". If the former interpretation is adopted, the Competition Tribunal would possess identical remedial jurisdiction at both the preliminary and final order stage, excepting of course the time limited nature of the interim order. To summarize, it is submitted that the relief that would be available would be broader than the wrong sought to be enjoined. Consequently, if the "substantial impairment" criterion is retained is S.72(1)(a), it is recommended that the final phrase in section 72(1) be amended to read, "...toward the completion or implementation of the proposed action."

It is certainly reasonable that the duration of the preliminary injunction obtained ex parte be less than that obtained by way of notice of motion. In addition, it would seem desirable that an interim order obtained for non-compliance with the pre-notification provisions should continue until the conditions have been satisfied[446] and the Director has been afforded the "ordinary waiting" period to analyze the data. Although this is stated in S.72(5), it is submitted that the subsection should be rewritten to avoid any possible ambiguity.

Of questionable merit is the rationale for the inclusion of subsection 72(6). If it is accepted that the essence of the entire section is to provide a brief interlude within which the Attorney-General may initiate proceedings, in the general case, or garner more information, in the notifiable transaction case, then one is compelled to express doubt about the objective of subsection 72(6). If the Crown declines, for whatever reason, to proceed under section 64 within the statutorily imposed limitation periods governing the duration of the preliminary injunction, the merger may proceed as previously planned. The Crown is barred from extending the operational period of the preliminary order. It is suggested that the limitation periods themselves act as strong inducements on the Crown to proceed expeditiously, otherwise the ability to hold the merger "in neutral" is lost. Thus, a real and effective incentive exists for the Director to commence proceedings before the injunction expires.

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[446] Ibid., S.93 and 94 respectively.

One must question the practical impetus that subsection 72(6) has on expediting proceedings. If the Director does not "proceed as expeditiously as possible to commence" proceedings, what remedies rest with the respondents? In response to any action taken by the respondents, the Director could quite easily argue that his Department was proceeding to collect information and consider the matter. In a situation where the Director does commence proceedings within the period of the order, the Director is already under a common law duty to complete the action within a reasonable time. Because the preliminary injunction is only available in pre-application situations, the primary duty imposed on the Director should be to proceed to commence, surely not complete, proceedings under section 64. Moreover, a moderate risk remains that the subsection would be construed by the Tribunal in such a manner as to require the Director to commence proceedings whenever a preliminary injunction is granted. If the Director, upon application for a preliminary injunction, were also under a positive duty to institute formal proceedings under section 64, then the net effect would be to coerce the Director into making his decision to proceed before he has adequately considered the information supplied. In effect, the purpose of the extended "waiting period" available under the pre-notification provisions would be circumvented. This stricture on the Director would result if the section were construed so as to compel the Director, on application for a preliminary order, to commence an action. However, the Tribunal may emphasize the word "proceed" in the subsection and consequently require the Director only to take steps towards the commencement of proceedings.

Under the principles enunciated at common law, if the successful applicant for an interim injunction subsequently withdrew the principal action, he was deemed to have had a weak case; consequently, the applicant was liable to pay damages to the respondent on his undertaking. Under section 72, it would be highly unlikely that the Crown, being the applicant, would be obligated to pay damages for enforcing the public interest. Therefore, it is more probable that the Attorney-General would apply for a preliminary injunction simply to compile information and analyze the situation rather than enjoin the merger with the intention of commencing an action.

In summation, it would have been advisable for subsection 72(6) to be deleted entirely. This step would not have diminished the desired positive duty on the Director to avoid delay. Coincidentally, the omission may have avoided the ambiguity over whether the Director was required to apply, as a condition subsequent to the granting of a preliminary injunction, for an order under section 64.

Finally, it must not be overlooked that the preliminary injunction pursuant to section 72 is only available for proposed, not completed, mergers. Unless an unusual situation arises where the proposal itself creates a dimunition of competition, the order will be in the nature of an injunction quia timet. When the Tribunal is faced with the task of interpreting the burden of proof intended by the phrase "reasonably likely", a strong incentive may exist to analogize to the common law jurisprudence.[169] The courts, forever cautious in granting relief before the injury has occurred, have in the past imposed a burden of proof which was more onerous than the conventional preponderance of evidence.[170] The Director may be forced to delay the application until the facts substantiate an uncontestable lessening of competition; by this time, the plans for the proposed merger may be so advanced that the maximum twenty-one day restraining order may not be sufficient to effectively halt the merger. The practical implication of superimposing the common law principles onto section 72 may be a reluctance on the part of the Director to employ the preliminary injunctive remedy; the Director might be well advised to immediately commence an action under section 64 and contemporaneously apply for an interlocutory order pursuant to section 76.

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[169] See: supra, discussion on common law jurisprudence governing injunctions quia timet, at Chapter VII D-2 and D-4.

[170] See: supra, Fletcher v. Bealey, n. 83; Earl of Ripon v. Hobart, n. 86.

3 INTERLOCUTORY INJUNCTIONS

(a) Procedure

In order to make application under section 76 of the Competition Act for an interlocutory injunction, the Director must have previously instituted proceedings under section 64.[171] In this context, the interlocutory remedy is a "post-application" procedure. As well, the interlocutory remedy is the only provisional or temporary relief available in the several instances which are listed below:

1. The merger has been completed,
2. The Director has made a previous application under section 72,
3. The Director is applying under a reviewable practice provision in Part VII other than the merger provisions, or
4. Damages have been realized.

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[171] Competition Act, S. 76(1).

Consequently, the procedure must be sufficiently broad and flexible in scope to entertain, for example, applications enjoining abuses of dominant positions under section 51 or specialization agreements under section 58.

The interlocutory provisions embodied in section 76 Competition Act are as follows:

> 76.(1) Where an application has been made for an order under this Part, other than an interim order under section 72, the Tribunal, on application by the Director, may issue such interim order as it considers appropriate, having regard to the principles ordinarily considered by superior courts when granting interlocutory or injunctive relief.
>
> (2) An interim order issued under subsection (1) shall be on such terms, and shall have effect for such period of time, as the Tribunal considers necessary and sufficient to meet the circumstances of the case.
>
> (3) Where an interim order issued under subsection (1) is in effect, the Director shall proceed as expeditiously as possible to complete proceedings under this Part arising out of the conduct in respect of which the order was issued.

As a result, the legislation transplants "the principles ordinarily considered by superior courts when granting interlocutory or injunctive relief"[172] into the bill. The courts are afforded equitable discretion in granting an interim order on terms necessary and sufficient to meet the circumstances of the case.[173] As in all other recent injunctive provisions, the Director is under an expressed duty to proceed to complete as expeditiously as possible.[174]

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[172] Ibid.

[173] Ibid., S. 76(2).

(b) Comparison of S. 76 Competition Act and S. 29.1 Combines Investigation Act

The general principles governing the issuance of interlocutory injunctions have been outlined in detail in the discussions above on common law jurisprudence. However, it is necessary to highlight the divergence in the procedures enacted in the Combines Investigation Act from the ordinary doctrines governing the availability of interlocutory injunctions and therefore relief under S.76 of the new Act. Although the rules for service may differ from province to province, the general thrust of the regulations seem in concert with the codified standards enunciated in section 29.1 Combines Investigation Act. The fundamental distinction between the two relief procedures emerges upon examination and comparison of the tests to be satisfied. The first of the two-pronged tests under the Combines Investigation Act[175] appears to be an attempt to enact the prima facie strength of case doctrine discussed at length in American Cyanamid.[176] It is arguable whether the burden of proof required under the former Act was heavier than the common law requisite. In tandem with predicting the probability of the applicant's ultimate success at trial, the Combines Investigation Act required that the risks of uncompensatory harm to persons named in the application be weighed.[177] This balancing mechanism is strikingly similar to the principle of the balance of convenience employed in the case law.[178] The alternate secondary ground in the former Act requiring proof of "injury to competition"[179] was unique to the interim injunction provisions in the Combines Investigation Act.

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[174] Ibid., S. 76(3).

[175] Combines Investigation Act, S. 29.1(1)(a).

[176] Supra, n. 98.

Under either the former legislation or the common law principles the order may be granted ex parte; however, the Combines Investigation Act restricted the duration of the order to not more than ten days. Both procedures allow the ex parte order to be varied for any definite period.

Finally, the common law requirement that the plaintiff indemnify the respondent for damages resulting from the failure of the plaintiff to prove his case induces the plaintiff to mitigate damages by avoiding delay in proceeding to trial. Due to the impracticality of requiring similar undertakings of the Crown, both the former legislation and the Competition Act have imposed a positive duty on the Director to proceed expeditiously to *complete* proceedings. This adoption of subsection 29.1(6) Combines Investigation Act into subsection 76(3) Competition Act may not be as troublesome as its inclusion in the preliminary injunction provisions due to the fact that the proceedings must already have been commenced.

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[177] Supra, n. 175, S. 29.1(1)(b)(ii).

[178] Conceptual distinction does exist. Under the common law doctrine the applicant was also the potentially injured plaintiff; under the Combines Investigation Act, the applicant is the Attorney-General, while the injured part may have been any person named in the application.

[179] Supra, n. 175, S. 29.1(1)(b)(i).

(c) Comparison of S.76 and S.64 Competition Act

At the preliminary stage, the courts are predisposed not to pre-try the case on its merits. On the other hand, an integral interest in assessing the appropriateness of interlocutory relief must encompass the probability of the plaintiff's final success. In evaluating the acceptability of the merger, the courts must apply the substantive test of review employed in the substantive provisions, namely, whether "the merger or proposed merger prevents or lessens, or is *likely* [emphasis added] to prevent or lessen, competition substantially".[180] All the defences available to the defendant at trial will also be available to the respondent on application for an interlocutory injunction. Consequently, section 76's operational viability, which relies on its ready availability must rest on the degree of proof imposed on the applicant. Although the jurisprudence which has developed since the landmark case of *American Cyanamid* may support the premise the something less than a prima facie case need be proved, the case law does not unanimously endorse a weakened burden of proof. In addition, it must be appreciated that the crucial element in the evaluation of the balance of risk requires a global or aggregate prediction of the probability of anticompetitive consequences. This requirement may outweigh any perceived advantage the applicant may have enjoyed in proving only a "real prospect" of success. In sum, it is submitted that the applicant for an interlocutory injunction will be obliged to prove elements identical to those for final relief: the proposed merger is likely to lessen competition substantially and is not exempt by reason of a statutory defence provision.

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[180] Competition Act, S.64(1).

(d) Comparison of sections 76 and 72 Competition Act

The Competition Act is unique in the long history of proposed competition reform in its inclusion of two separate formulae which provide provisional injunctive relief. In capsule form, the merger specific civil procedure of section 72 provides the opportunity to extend the pre-notification "waiting period"; the generally applicable principles of ordinary interlocutory relief enacted in section 76 strive to afford a temporary pre-trial preservation of the status quo. From a policy perspective, the question arises whether one of the two sections will be favoured by the Director, the other being consigned to a subordinate, or perhaps superfluous, role.

For ease of comparison, the summary below outlines the major comparable and distinctive elements of these two provisional injunctions:

MATTER	PRELIMINARY INJUNCTION: S.72 COMPETITION ACT	INTERLOCUTORY INJUNCTION: S.76 COMPETITION ACT
1. Adjudicative Body	1. Tribunal	1. Tribunal
2. Applicant	2. Director	2. Director
3. Respondent	3. Person named in application	3. Subject to Rules of Court
4. Type of Merger	4. Proposed	4. Proposed or Actual
5. Merger Specific?	5. Yes	5. No
6. Application under substantive provisions	6. No application may have been made	6. Must have made application
7. Burden	7. "reasonably likely"	7. Strength of case - less than *prima facie*
8. Effect on Competition	8. No defences	8. Defences available
9. Additional Elements of Test	9. Irreversible harm "likely"	9. Balance of convenience
10. Non-compliance	10. With S.86	10. Not addressed
11. Notice	11. 48 hours	11. Rules of Court
12. Dispensation	12. (a) not reasonable (b) exigent	12. Rules of Court
13. Duration of Order	13. (a) ex parte - 10 days (b) on notice - definite	13. (a) ex parte - definite (b) on notice - definite
14. Extensions	14. Not Available	14. Available
15. Duty of Director	15. to proceed	15. common law duty

to complete

Fundamentally, the preliminary injunction is intended to enjoin proposed mergers at the pre-application stage, whereas the interlocutory injunction requires as a prerequisite the commencement of proceedings under Part VII. However, section 72 does not appear to be restricted to pre-application situations. The Crown's preference between the two procedures will likely be determined, therefore, by the prospects for a successful application. This matter will ultimately rest on two factors:

1. The elements of the test to be satisfied, and
2. The degree of burden of proof which must be overcome.

With respect to the first factor, both the preliminary and interlocutory injunctions require that the applicant prove that a substantial lessening of competition likely result from the merger or proposed merger. However, the test for an interlocutory injunction impliedly makes available to the respondent all the defences to a section 64 proceeding. Consequently, an examination of the primary grounds for obtaining a temporary injunction would indicate a tentative propensity on the part of the Director to favour section 72. However, the secondary grounds cast a shadow on this implication. Under section 76, the Crown must prove that the balance of convenience lies with the applicant; this task would seem to be encumbered with less uncertainties than the secondary ground pursuant to section 72. Section 72 requires proof of an action which is likely "to substantially impair the ability of the Tribunal to remedy the effect of the proposed merger on competition under section 64, because that action would be difficult to reverse."(8) To this point, the Director should have no clear preference.

It is submitted that the second determinative factor, regarding the requisite burden of proof, will effectively demonstrate the uses of the two sections and the Director's choice between them. Although the analysis must be speculative at this stage, it appears highly probable that the burden of proof pertaining to the preliminary injunction provisions will be for all practical purposes on the balance of probabilities. The justifications for such an assertion are twofold: First, the express burden governing the secondary ground of irreversible action is undeniably a likelihood of impairment. Nonetheless, the primary ground, which considers the anticompetitive effect of the proposed merger, pivots on the innovative wording "reasonably likely". This terminology may be interpreted in a manner which connotes something less than a probability, in an attempt to make temporary relief more readily attainable. Notwithstanding this view, in the context of the relatively onerous burden applied (in the jurisprudence) to injunctions quia timet, it seems more conceivable that the phrase would merely dampen the otherwise strong probability requirement. On balance, the burden which the Crown could expect to face on a section 72 application would presumably reflect the ordinary civil measure.

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(8) Competition Act, S. 72(1)(a).

With respect to the effective burden applicable to interlocutory injunctions, the requisite degree of proof must correspond with the burden espoused in the case law. On a perfunctory application of the ratio in American Cyanamid, it would appear that the strength of the applicant's case need not be prima facie but merely exhibit a "real prospect" of success. Accordingly, the evidentiary burden being less than that required under section 72, the Director would favour proceeding under section 76 for an interim order, particularly since the order would not be limited to a maximum of twenty-one days. Procedurally, the Director would be obliged to commence an action under section 64 and then make application for provisional relief by way of section 76.

The elementary question may be summarized as follows: Upon application for interlocutory relief, should the applicant be required to prove a prima facie case? From a strictly theoretical perspective, an slight preference would seem to rest with the negative response. The merits of the case should be decided at trial on the balance of probabilities; the law should impose a lesser burden on the applicant in order to escape imminent irreparable injury while awaiting the adjudication of the matter. The principal objective of an interlocutory injunction is to avoid the risk of harm to the parties pending litigation, not to preempt the final disposition. In the alternative, one may argue that if the burden of proof were identical on interim application and at trial, the courts would be compelled to rely upon the balance of convenience doctrine to reconcile the issue. In practice, a comparison of the probable damages to the public interest and the parties to the merger may prove exceedingly difficult; a weaker burden evidencing the strength of the applicant's case could avoid such an irreconcilable comparison of damages. A fortiori, if any facts are in dispute, a scenario which is highly probable in a merger action, the credibility of the evidence and the weight to be attached thereto should not be decided at trial, although separately and independently of the substantive anticompetitive issue.

In addition, evidence on an interlocutory motion is lead by way of affidavit; the assertions in the deposition need only be on belief, not knowledge, touching the matters in question. As a consequence, it may be unreliable to ascertain the strength of the plaintiff's case on such statements which are not subject to the ordinary rules of evidence.

Finally, the courts may have been predisposed to endorse the balance of convenience approach because the risk of harm could be mitigated by requiring the plaintiff to undertake indemnification. Unlike private plaintiffs, the Director may not be subjected to such undertakings if he sues in the public interest.[112] Although this Crown privilege could support an argument for greater reliance on proving a prima facie case, it is notable that the Crown may sue with impunity in many instances. For example, in any criminal prosecution, the Crown is not liable to compensate an accused who is ultimately acquitted. In sum, until the law is established under section 64, the courts will simply be unable to predict the ultimate probability of success at trial and therefore will be extremely recalcitrant in granting an interlocutory injunction unless the burden of proof on the applicant is something less than a prima facie standard. For the preceeding reasons, the burden of proof established in American Cyanamid appears to be justified.

However, the opposing argument would limit the doctrine in American Cyanamid and elevate the prima facie test. A matter of vital concern is the effect that the injunction may have on the design of the parties to complete the merger. If the practical outcome of the provisional order is to discontinue the merger, then the issue may never go to trial; accepting this high risk in some cases, it might be advisable to evaluate the plausibility of the applicant's contentions at the preliminary application stage. Moreover, depending on the interpretation attributed to subsection 76(3), the Director may never advance the proceedings to the trial stage. The option certainly appears to be open for the Director to withdraw or stay proceedings.

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[112] See: Discussion supra, Chapter D-4, on the ordinary principles of provisional injunctive relief.

Secondly, a very convincing argument for weighting the stature of the allegations more heavily emanates from the opportunity in Canadian jurisdictions to cross-examine on affidavit evidence. In the United Kingdom, the parties adverse in interest are not at liberty to challenge the credibility and veracity of the evidence. The fact that the deposition evidence supporting the strength of the case in American Cyanamid was placed before the court uncontested by cross-examination would have almost certainly influenced the court to diminish the persuasive weight to be attached thereto.

The underlying factor which appears to heighten the receptiveness of the courts to grant interim relief is the obligation on the plaintiff to undertake compensation in the event the preliminary expectations are not corroborated at trial. One method of guaranteeing this equitable counterbalancing mechanism would be to compel the Director to indemnify the parties in case of loss. Unfortunately, neither the jurisprudence[123] nor political intuition will justify the imposition of this covenant on the Crown when acting to protect the public interest. Consequently, there is no cost to the Director if an order is granted and the respondents successfully defend against the allegations at trial. The absence of undertaking indemnification weakens the usefulness of the balance of risk approach and strengthens the proposition that a prima facie case should be established in order to enjoin the merger. In any event, the balance of risk test must overcome a more intrinsic problem; injury to competition and the economy as a whole must be compared to damages suffered by the parties enjoined by the injunction.

Although a careful reading of American Cyanamid does not support the equating of "real prospect" and prima facie by Mr. Justice Steele in the Carlton Realty case,[124] the amalgamation of the strength of case with the balance of risk principles leads one to the unavoidable conclusion that the courts will desire proof of a prima facie nature. The determination that the risk or probability of harm would lie with the applicant would necessarily entail proving a presumptive case in favour of the Director. If the merger is effectively barred as a result of the granting of an interlocutory injunction, the two-fold standard espoused by Lord Diplock in N.W.L. Ltd. v. Woods[183] which elevates the prima facie test to its pre-American Cyanamid position should be required. The harm would be complete. Furthermore, because the Director would not be compelled to compensate the parties, Lord Diplock's criterion of adequate monetary recompense would also not be fulfilled.

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[123] See the discussion on American Cyanamid, supra, at n. 98, and accompanying text.

[124] Supra, n. 113.

It seems plausible that the inevitable reliance on the strength of case test, in one form or another, would persuade the Tribunal to apply the ordinary civil burden of proof on applications for interlocutory relief. To require a lesser burden would always prejudice the respondents. The result would be that only certain private commercial enterprises would bear the cost of preserving a competitive environment for the entire society. It is granted that this argument has not prevented the development of the criminal law, with its potential for wrongful accusation; however, the probability of wrongful public scrutiny is much higher for the ever increasing number of large mergers in Canada.

If the jurisprudence develops as proposed above in a direction which ultimately relies on the evaluation of the potential prospects of the applicant's case, the intended purpose of the interlocutory relief provisions will be effectively obstructed. The Director may be enticed to rely on the precarious provisions available under section 72. The first challenges under the provisional injunction provisions may attempt to have defined the "reasonable likelihood" burden in section 72. If the Tribunal interprets the burden to be weaker than the balance of probabilities test, then the Director may be forced to utilize these provisionals for situations other than extending the prenotification "waiting period". This would be an unfortunate misdirection of the public policy intentions.

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[183] Supra, n. 117.

F RECOMMENDATIONS

1. Preliminary Injunctions: S. 72 Competition Act

Assuming the primary intention of section 72 is to extend the "waiting period" imposed by the pre-notification provisions, it might be highly advantageous to restrict the availability of the preliminary injunction to only those transactions subject to the pre-merger notification and information requirements. This might entice the Tribunal to interpret liberally the test for availability and the respective standard of proof to be applied.

It is recommended that the burden of proof be explicitly defined in such a manner that obviates the requirement that the applicant prove a _prima facie_ case. This objective could most easily and effectively be accomplished by explicitly exempting the necessity of substantiating a _prima facie_ case. Conjoined with the "reasonable likely" standard contained in paragraph 72(1)(a), this express exclusion would clearly indicate to the courts and the Tribunal the legislators intention to limit the burden on the applicant. Alternatively, the burden could be phrased in terms of possibilities rather than likelihoods. Either approach would more closely approach the purpose of preliminary relief.

With respect to the test itself, it is not self-evident why the secondary ground is required at all. If the objective of the provision is to provide a readily accessible means of temporarily enjoining a potentially anticompetitive merger while the Director assesses the situation, the fact that the Director may ultimately be capable of remedying the anticompetitive effect by use of an order under section 64 appears to be completely misdirected and immaterial. It is submitted that the major issue on application for injunctive relief should be the possibility of anticompetitive effects of the merger; an interim order to hold the parties separate and apart would still permit the parties to proceed with the preparation of the merger and mitigate any damages which might arise as a result of the injunction.

In the alternative, if the entire secondary ground is not deleted, it may be advisable to delete the second prong of the test requiring substantial impairment to the Tribunal to subsequently remedy the anticompetitive effect of the proposed merger under section 64. As noted above, a subsequent ability to "untie the knot" does not seem consistent with the principal purpose of the section to lengthen the pre-notification "waiting period". The provision should focus on enjoining a potentially irreversible action which is being taken to advance an anticompetitive merger.

Due to a strong suspicion that subsection 72(6) is merely a holdover from its counterpart, subsection 29.1(6)

Combines Investigation Act, and the realization that its inclusion fosters several potential pitfalls which are not counterbalanced by any new protection of the rights of the merging parties, it might well be expedient to delete the entire subsection. The inclusion of subsection 72(6) appears, in the context of the pre-notification procedure, to impose a duty on the Director which is conspicuously absent from the conceptual thrust of the notifiable transaction requirements.

2. Interlocutory Injunctions: S. 76 Competition Act

The ultimate goal of injunctive relief is to provide a remedy to prevent the irreversible comingling of the merging parties prior to a final determination of the suitability of the proposed merger on the merits. This prophylactic aspiration can only be satisfied if the prevention is less difficult to acquire than the cure. Unfortunately, any success in enjoining a proposed transaction by means of the interlocutory injunctive provisions rests, in the final analysis, on the operational outcome and judicial interpretation of the substantive merger provisions.

From a purely procedural perspective, the Crown will conjunctively initiate an action under section 64 and apply for an interlocutory order. Unless the Director were to commence proceedings *mala fides*, the Director would be in the unenviable position of being prepared to substantiate a substantial lessening of competition and to negate the defences and exemptions accompanying the substantive test _before_ or at least _concurrently_ with an application for provisional relief. Furthermore, it is not beyond the realm of possibilities that the application itself could extend for such a protracted period of time that the merger could be consummated in the interval.

Notwithstanding the status of the Director's case under section 64, it is highly improbable that the Tribunal would decide the matter without regard to the strength of the applicant's case. One must not lose sight of the predisposition of the courts, therefore possibly the Tribunal, to favour _ex post_ remedies in damages rather than _ex ante_ intervention by way of orders in the nature of prohibition.

The consequence of this duty on the Director is to frustrate any attempt to recommend alternate means of strengthening the operational effectiveness of section 76 without modifying significantly the fundamental policy manifest in section 64. Although one might venture to recommend provisions which would negate the duty of proving a _prima facie_ case or would remove the availability to the respondent of the defences or exemptions, such statutory overrides of the developed jurisprudence are highly improbable. In short, the success of obtaining an interim order is directly correlated with the probability of proving the merits of the action.

VIII THE MEASUREMENT OF COMPETITION AND ITS APPLICATION TO PROVISIONAL RELIEF

A THEORIES OF DISPERSION AND COLLUSION

The apportionment of economic activity amongst the members of a specifically defined market has, since Joseph Bain's influential treatise on Industrial Organization,[1] raised the question of the relationship between the structure of the industry under scrutiny and the behaviour and performance of the constituent firms. Concentration, in its basic form, is a measure of the proportion of the pertinent market production which is supplied by a few large firms. Two primary parameters are determinative of the level of concentration attributable to the market under observation:

(a) The number of firms in the market, and

(b) The dispersion or level of equality (or inequality) amongst the members.

If one assumes that all firms in the market are of equal size in terms of output or sales, then a decrease in the number of producers must *ceteris paribus* increase the concentration of any particular set of suppliers. The corollary of this observation implies that for an equal number of firms in two separate markets, the market which has the greater inequality in firm size will exhibit a higher concentration level. Although exceptions to the second proposition may exist,[3] in most cases a decrease in the number of competitors or an increase in the dispersion amongst the firms will generate an increase in concentration. The perplexing issue focuses on the link between concentration and competition; the economic literature is not convinced that an increase in concentration necessarily leads to anticompetitive behaviour and suboptimal economic performance.

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[1] See: J.S. Bain, Industrial Organization. (2d) New York: John Wiley & Sons, (1968) at p. 430 *et seq.* for the seminal development of the structure - conduct - performance paradigm of industrial organizations. See also: C. Green, Canadian Industrial Organization and Policy. Toronto: McGraw-Hill, (1985) at p. 47.

Turning first to the relationship between the number of firms in the market and the resultant effect on competition, the mainstream view posits a positive correlation. A decrease in the number of firms may lead to a decrease in the existing competitive nature of the industry for the following reasons:

(a) A decrease in the transaction costs of collusion. Negotiation and enforcement of the arrangement becomes less difficult and costly,

(b) A decrease in the difficulty of judging the probable reaction of rivals,

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[3] For example: Market A may consist of one firm with a market share of 50 percent and fifty fringe firms each contributing one percent each. Market B may comprise four equally sized firms. Obviously, Market B, which exhibits less dispersion, has a higher CR4.

(c) A decrease in the disciplinary efforts of non-members or fringe firms, and

(d) An increase in the probability of conscious parallelism.

It is emphasized at this point that a decrease in the number of firms which yields an increase in concentration need not necessarily create anticompetitive repercussions. An increase in market concentration may result in an effective counterbalancing of a dominant firm, increase inter-firm strategic rivalry, or it may induce an increase in supply substitutability.[3] As it is impossible to choose a concentration measure which would differentiate between circumstances which would trigger either an increase or a decrease in competitive behaviour, one is compelled to opt for one of the alternatives. Due to the relative frequency of tacit collusion and the intuitive appeal of the transaction cost analysis, it is recommended that a concentration index which infers anticompetitive effects from a decrease in the members of a market is preferable.

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[3] Note: An increase in supply substitution, including entry de novo, "toehold" expansion or perceived potential competition, is incorporated in the analysis at the market delineation stage in the guidelines proposed in this paper. Consequently, the issue addressed must presuppose the correct product and geographic market and justify an increase in competition solely on a diminution in the number of firms.

With respect to the correlation between firm output inequality and performance, the desired functional relationship is not as evident. Two opposing theoretical constructs emerge: one postulates that inequality of firm size induces less competition and antitrust suspicions, while the other proposes that equality of member firms facilitates collusion and anticompetitive behaviour. The former "dispersion hypothesis" appears to be premised on the theory of "dominance"; the market leader is capable of bending the other member firms to follow its will.[4] A potential problem with this concept may develop in an ologopolistic market structure. For example, an oligopoly consisting of three equally sized large firms with an insignificant competitive fringe may be highly competitive, even though there is no dispersion amongst the large firms. It is also surmised that the success of predation is contingent on disparity;[5] this rationale is challenged by proponents of the "Chicago School".[6] A third justification for the acceptance of the dispersion hypothesis is rooted in the theory of price leadership:

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[4] Neil B. Cohen and Charles A. Sullivan, "The Herfindahl-Hirschman Index and the New Antitrust Merger Guidelines," (1983) 62 Texas Law Review 453, at p. 492 et seq.

[5] Areeda and Turner, "Predatory Prices and Related Practices Under Section 2 of the Sherman Act." (1975) 88 Harvard Law Review, 697, at p. 698.

[6] R. A. Posner, "The Chicago School of Antitrust." (1979) 127 University of Pennsylvania Law Review 925 at p. 939.

> Of the several varieties of oligopolistic coordination, "price leadership" would seem to be the most likely candidate to justify the HHI theoretically."[7]

Scherer defines price leadership as follows:

> Industry practices or customs under which list price changes are normally announced by a specific firm accepted as the leader by others, who follow the leader's initiative.[8]

Several problems accompany the use of price leadership to justify the dispersion theory. First, the price leader may simply be the organization with the lowest costs.[9] Second, it is possible to have a price leader when the dispersion of firm size is small.[10] Third, the different sized firms may be faced with different cost curves which would result in divergent perceptions of the optimal price.[11] However, the most perplexing and controversial shortcoming of the dispersion theory resides in its inability to explain the phenomenon of tacit collusion or conscious parallelism.[12]

The theory of collusion, the antithesis of the dispersion theory, asserts that an increase in equality, rather than inequality, of firm size will predispose the industry to anticompetitive behaviour and allocative inefficiency. The rationale for this supposition seems to be fourfold:

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[7] Supra, n.4, at p. 496. See also: P. Areeda Antitrust Analysis, Boston: Little, Brown and Co. (1981) at par.262(e); Scherer, Industrial Market Structure and Economic Performance, Chicago: Rand-McNally, (1970), at p. 167.

[8] Ibid., Scherer, at p. 176.

[9] Ibid., at p. 167.

[10] Spivack, "New Merger Guidelines are Substantially Different" August 2, 1983, Legal Times, p. 38.

[11] See: D. Baker and W. Blumenthal, "The 1982 Guidelines and Preexisting Law". (1983) 71 California Law Review 311.

[12] See: W.T. Stanbury and G.B. Reschenthaler, "Oligopoly and Conscious Parallelism: Theory, Policy and the Canadian Cases," (1977) 15 Osgoode Hall Law Journal, 617.

(a) The firms may have similar cost curves and consequently entertain comparable perceptions of the optimal price,[13]

(b) It may be more evident that one of the members of the industry is "cheating",

(c) Transaction costs to maintain the concerted behaviour may be lower, and

(d) Concensus as to price leadership may be more readily available.

It remains an outstanding and unresolved paradox whether the dispersion or collusion viewpoints provides the appropriate theoretical foundation for antimerger policy.

It has been argued rather persuasively[14] that consciously parallel behaviour rarely,[15] if ever, occurs without definite concomitant "plus factors". These plus factors may include the publication of suggested retail price lists, or the employment of trade associations, delivered pricing or rule of thumb pricing practices. The logical extension of this analysis is to infer that equality of market shares per se, without more, is not a sufficient condition for increased market power. In other words, a simple structural test is not sufficient; a behavioural analysis is required to determine whether an industry exhibiting a very low variance in market shares is prone to anticompetitive conduct and ultimately an enhancement of market power. If one accepts this supposition, the conflict existing between the dispersion and collusion theories may be less enigmatic in the context of administrative guidelines governing the Director's application for provisional or temporary injunctive relief.

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[13] Supra, n.4, at p. .

[14] Supra, n.12, Stanbury and Reschenthaler.

[15] The analysis suggested above assumes that the incidence of "pure" conscious parallelism is so infrequent, that to include this concept in merger guidelines would not be policy effective.

The principal objective of guidelines, which may be employed by the Director to ascertain whether to apply for a provisional injunction, is to provide an efficacious, incomplicate, prima facie determination of the effect of a merger on market power. If the Director were required to evaluate the behavioural arrangements of the industry in question in assessing the probability of success at trial, expediency, predictability and simplicity would be sacrificed. From an alternate perspective, the possibility of the dispersion theory or dominant firm hypothesis not rendering correct anticompetitive implications is far less than the potential for misdirected policy decisions arising from the presumption that equality of market shares is undesirable. Consequently, as a preliminary guideline for anticompetitive performance, it is preferrable to adopt a structural test which monitors the dispersion in market shares, while tempering the analysis for blatant abuses of collusive behaviour.

B CONCEPTUAL APPROACHES TO GUIDELINE TESTS

Several conceptual approaches are available to measure the effect of a merger on industry performance and market power. The most acceptable from the economist's perspective is a "Rule of Reason" approach which would weigh all the relevant costs and benefits attributable to the acquisition. This method is extremely cumbersome and involved; it would have the practical effect of transforming a preliminary inquiry into a trial of the merits. Second, a per se rule of illegality above a specified threshold is appealing in its simplicity, but is inequitable and misleading in its application. The per se approach, similar in nature to absolute liability in a criminal context, would be unable to deal in a reasonable fashion with the propensity for collusive behaviour in an industry exhibiting low dispersion levels. Third, a per se rule allowing specified defences, similar in form to strict liability criminal offences, again would be inappropriate to deal effectively with the dispersion-collusion paradox. The final method, which will be utilized in the subsequent analysis, would employ a structural presumptive test of dispersion, the presumption being rebuttable by the merging parties or, in the case of collusion, reinforced by the Director. It must be underscored that this preliminary assessment is only to "guide" the Director in his determination of the feasibility of instituting proceedings for provisional relief; it is not to restrict his submissions on application nor is it to govern the ultimate determination of the acceptability of the merger on its merits.

C ALTERNATE MEASURES OF CONCENTRATION

Many measures are available, as a result of extensive economic research and interest in the area, which purport to correlate industrial performance to structural characteristics. Although it is not the intent of this discussion to critique the complex literature, it is instructive to highlight the more frequently mentioned estimates.

The ultimate goal is to measure the effect of industrial structure on market power resulting from a proposed merger. The simplest and most theoretically sound measure of market power is the Lerner index[16] (L) which measures the upper limit of the proportional deviation of the monopolistic price (Pm) from the competitive price (Pc). In essence, the Lerner index measures the relative size of the monopoly overcharge as:

$$L = \frac{P - MC}{P} \text{, P is monopoly price, MC is marginal cost.} \quad (1)$$

This index, which reflects the ability of a firm to set the price of the product above the competitive level, refers to:

> the proportional deviation of price at the firm's profit-maximizing output from the firm's marginal cost at that output.[17]

For the purpose of measuring market power, several difficulties arise with the use of the L-index. First and foremost, a practical problem perpetually exists in estimating the value of marginal cost. Second, the index overstates the proportional deviation of the monopoly price from the competitive price. Third, if price discrimination is present, several L-indexes will be required. Lastly, the L-index may underestimate market power because marginal costs may be high due to X-inefficiency. Aside from these shortcomings, the Lerner index provides a useful and justifiable benchmark to which concentration ratios may be correlated and evaluated. The Lerner index is not a measure of concentration nor a descriptor of market structure; it is a barometer of market performance to which the following concentration computations may be evaluated in terms of predictive reliability.

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[16] Lerner, "The Concept of Monopoly and the Measure of Monopoly Power" (1934) 1 Review of Economic Studies 157, at p. 169

[17] W. Landes and R. Posner, "Market Power in Antitrust Cases". (1981) 94 Harvard Law Review 937, at p. 939

The most accepted measure of concentration[18] is the concentration ratio, CRi, defined as:

> [T]he percentage of total industry sales (or capacity, or employment, or value added, or physical output) contributed by the largest few firms, ranked in order of market shares. The most common variant in American studies (referred to as the four-firm sales concentration ratio and often as the concentration ratio) is the percentage of total industry sales originated by the leading four firms.[19]

Algebraically, the CR4 is formulated as:

$$CR4 = \sum_{i=1}^{4} S_i ,$$

where Si is the market share of the ith firm. It has a range from zero for very low levels of concentration to unity for extremely high levels of concentration. Unfortunately, this simple measure of industry concentration is burdened with several limitations:

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[18] See: Scherer, supra, n. 7 at pp. 56-64, for an extensive and thorough discussion of the principal measures of concentration. See also: J.C. Hause, "The Measurement of Concentrated Industrial Structure and the Size Distribution of Firms." Winter (1977) Annals of Economic and Social Measurement 73; H. Hotelling, "The Selection of Variates for Use in Predication, With Comments on the General Problem of Nuisance Parameters." (1940) Annals of Mathematical Statistics 278; Almarin Phillips, "A Critique of Empirical Studies of Relations Between Market Structure and Profitability." June (1976) Journal of Industrial Economics 241; and Alice P. White, "A Note on Market Structure Measures and the Characteristics of Markets that They 'Measure'." October (1982) 49 Southern Economic Journal 542.

[19] Ibid., Scherer, at p. 56.

> To sum up, concentration ratios understate the true quantum of monopoly power when markets are defined to include nonsubstitutes, when meaningful markets are local or regional rather than nationwide, when sellers enjoy strong product differentiation advantages within relevant product lines, and when special institutional features (like the soft drink franchise pattern) intrude. The degree of monopoly power is overstated when substitutes are excluded from the industry definition and when import competition is significant.[20]

In addition to these error variables, the CR4 provides a measure of the market at only specified points. Such "discrete" indices may provide cumulative concentration curves[21] which provide conflicting relative levels of concentration for different markets depending on the number of firms chosen to define the concentration ratio.[22] Closely related to the concentration ratio is the Lorenz-Gini[23] approach which is a discrete index of firm-inequality.

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[20] _Ibid_., p. 64.

[21] The cumulative concentration curve is also known as the Lorenz Curve. See: Scherer, _supra_, n.18, at p. 57.
A graphic technique for summarizing the information in a concentration table is the Lorenz curve, which shows as a continuous function the percentage of total industry sales (or some other variable) accounted for by any given fraction of the total company population, with the firms ranked in order of market share or size. Lorenz curves can be characterized numerically by means of the Gini coefficient, which measures the departure between the Lorenz curve actually observed and the curve that would appear if all firms had equal market shares or sales. A Gini coefficient of zero indicates perfect equality of firm shares; a coefficient of 1.0 reveals total inequality (with the leading firm producing the entire output).
See also: Miller, at p. 597, n.4.

> The Lorenz-Gini approach has two main disadvantages. As an index solely of inequality, the Gini coefficient may suggest paradoxical inferences when an industry is occupied by a small number of evenly matched firms. The Gini coefficient for duopolists or triopolists with equal market shares is zero, but one could hardly conclude that monopoly power is absent in such cases. Second, the shape of the Lorenz curve and the value of the Gini coefficient are quite sensitive to errors in defining the number of firms in the industry. The more borderline firms one includes, the higher the indicated degree of inequality tends to be.[24]

Summary indices, in the same spirit as the Gini coefficient but without its flaws, attempt to incorporate the market shares of all the firms in the industry.[25] The Herfindahl-Hirschman index (HHI)[26] is defined as the sum of the squares of the market shares:

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[22] Bailey and Boyle, "The Optimal Measure of Concentration," (1971) 66 Journal of American Statistical Association 702.

[23] See: C. Gini Variabilia e Mutabilia (1912) 19.

[24] Supra, n. 18, at p. 57.

[25] See: John E. Kwoka, Jr., "The Effect of Market Share Distribution on Industry Performance," (1979) 61 Rural Economics and Statistics 101, for a good review of the alternate concentration measures.

[26] O.C. Herfindahl, Concentration in the U.S. Steel Industry . Doctoral Dissertation: Columbia University, (1950); A.O. Hirschman, "The Paternity of an Index," (1964) 54 American Economic Review 761.

$$HHI = \sum_{i=1}^{N} S_i^2 \qquad (2)$$

where N is the number of firms in the industry.

The characteristics and attributes of the HHI will be discussed at some length in the subsequent section.

Concentration measures which are very similar to the HHI and favoured by loyal pockets of economists are:

(a) Entropy Coefficient:[27]

$$E = \sum_{i=1}^{N} S_i \log_2 \left(\frac{1}{S_i}\right) \qquad (3)$$

(b) Hall-Tideman Index:[28]

(c) Comprehensive Concentration Index:[29]

(d) Variance-Index:[30]

$$V = \frac{\sum_{i=1}^{N} (\log S_i - \log \overline{S})^2}{N}$$

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[27] H. Thiel, Economics and Information Theory (1967); Finkelstein and Friedberg, "The Application of an Entropy Theory of Concentration to the Clayton Act," (1967) 76 Yale Law Journal 677; C. Marfels, "The Consistency of Concentration Measures: A Mathematical Evaluation," (1972) 12 Zeitschrift Staats 196; I. Horowitz, "Numbers-Equivalents in U.S. Manufacturing Industries: 1954, 1958 and 1963," (1971) 37 Southern Economics Journal 396.

[28] Hall and Tideman, "Measures of Concentration," (1967) 62 Journal of the American Statistics Association 162.

[29] Horvath, "Suggestions for a Comprehensive Measure of Concentration," (1970) 36 Southern Economics Journal 446; Dansby and Willig, "Industry Performance Gradient Indexes," (1979) American Economic Review 249.

(4)

Although each of these measures has minor advantages and disadvantages when compared to the HHI, the quantum leap in the choice of a comprehensive concentration measure occurs when one shifts focus from the discrete indices such as the CR4 to the summary indices exemplified by the HHI. As Scherer concludes:

> Certain theories do support a definite preference. Nevertheless, theory provides conflicting guidance. As we shall see, there are hypotheses suggesting that for a given number of sellers, greater equality of market shares is conducive to coordinated monopolistic behavior, but other hypotheses imply that inequality fosters leadership and hence monopolistic behavior. A degree of open-mindedness seems appropriate, especially in view of the fact that the nonlinear properties of the often-preferred H index can be emulated by transformations of simple indices such as the four-firm concentration ratio. Pragmatism must also enter in for, in many instances, concentration ratio data are available in greater abundance, or at a higher level of accuracy than, say, H indices or the information needed to compute them.
>
> Except when fine distinctions must be made, which market structure measure one uses may not be a matter of great moment, since the leading contenders tend to yield similar industry rankings and have highly correlated numerical values.[31]

D THE CHARACTERISTICS OF THE HERFINDAHL-HIRSCHMAN INDEX

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[30] P.E. Hart and S.J. Prais, "The Analysis of Business Concentration," (1956) Journal of the Royal Statistical Society 119 Series A 150,

[31] Supra, n. 18, p. 58.

The Herfindahl-Hirschman index (HHI), as defined above in equation (2), is a summary measure of market concentration which has been heralded in the economic literature as a more comprehensive yardstick than the familiar four-firm concentration ratio (CR4). Because of this preferability, it is instructive to outline the properties of the HHI. Recollecting the formal definition as:

$$\text{HHI} = \sum_{i=1}^{N} S_i^2 \text{, where } S_i \text{ is the market share of the } \underline{i}\text{th firm,} \qquad (2)$$

readily indicates that the range of the HHI varies from zero for highly unconcentrated markets to a maximum value of unity for monopolistic or highly concentrated industry.[32]

The major characteristics of the HHI become apparent upon analysis of the following relationship:

$$\text{HHI} = \sum_{i=1}^{N} s_i^2 + \frac{1}{N} \qquad (5)$$[33]

The term s_i^2 is merely the square of the market shares as measured as deviations from the mean, and the symbol N represents the number of firms in the industry. This extremely influential result illustrates the effect of the number of constituent firms in the market and the degree of dispersion amongst the firm's market shares on the measure of market concentration. First, as the number of firms in the relevant market decrease, the HHI must increase. Assuming the HHI is positively correlated to concentration levels and that such concentration levels are indirectly related to the level of competitive behaviour, one must deduce that a decline in the number of firms resulting in a decrease in competition will be measured by an increase in the HHI. Second, as the level of dispersion amongst the member firms increases,[34] the HHI will also increase; assuming as above a positive relationship between the HHI and concentration and an inverse correlation between concentration and competition, a decrease in competition will be reflected through the HHI by a decrease in equality of firm size. In sum, a decrease in the number of firms or an increase in dispersion will imply an increase in market power as measured by the HHI.

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[32] Note: The convention has developed to express the HHI in terms of percentages rather than fractions. Consequently, the range of the HHI covers the values zero (unconcentrated) to 10,000 (monopoly). The effect of this convention is to simply multiply the HHI by 10^4 or sum the squares of the market shares expressed in percentages. For example, the HHI for a duopoly would be $(50\%)^2 + (50\%)^2 = 5{,}000$.

[33] The mathematical proof of this equation is found in Appendix E.

In addition to including all the market shares in the computation, the HHI, as suggested by the examples below, gives greater weight to the larger firms than to the smaller, and at an increasing rate.

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[34] Richard A. Miller, "The Herfindahl-Hirschman Index As A Market Structure Variable: An Exposition for Antitrust Practitioners," Fall (1982) 27 The Antitrust Bulletin 596.

	Industry						
	A	B	C	D	E	F	G
S_1	40	50	60	70	80	86	90
S_2	30	25	20	15	10	7	5
S_3	30	25	20	15	10	7	5
HHI	3,400	3,750	4,400	5,350	6,600	7,494	8,150.

Assuming the HHI accurately correlates concentration and market power, the HHI indicates that market E would have twice the market power as industry A. To reinforce this point, a recollection of equation (5), *supra*, clearly illustrates that a squaring of large market shares will augment the HHI to a greater degree than a corresponding squaring of a small market share. This emphasis on large market shares requires the acceptance of the dispersion theory to justify the application and use of the HHI to track market power. As one of the two simultaneous co-founders of the index concluded:

> The inventor of the index, A.O. Hirschman, emphasized that it embodies two aspects of the distribution of S_i in an industry: (1) the variation or dispersion in S_i (i.e., whether they are spread out-dispersed-or whether they are bunched-similar in value), and (2) the number of firms. He thus distinguished his index from similar indices, like the Gini coefficient, which measured only the first of these two aspects. Both aspects should somehow be

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[38] *Ibid.*, at p. 597.

included in a measure of industrial concentration.[36]

The HHI can be viewed as the weighted sum of the market shares, the weights being the values of the respective market shares themselves. The larger the market share, S_i, the larger the weight, S_i . Similarly, the HHI has been equated to the weighted sum of the slope of the tangents to the cumulative concentration curve.[37] This concept illustrates that the HHI is a specific subset of the Hannah and Kay index[38] (HKI) which does not presuppose any particular value to the weights:

$$HKI = \left(\sum_{i=1}^{N} S_i^{\alpha}\right)^{\frac{1}{1-\alpha}} \qquad (6)$$

where $\alpha > 0$ and $\Sigma S_i = 1$.

This formulation can be used to modify the weights to be attached to large and small firms. The parameter is an elasticity coefficient which, when large, will impose relatively greater significance to the larger market shares, and when small, will emphasize the influence of the proportionately smaller sized firms. The generalized form of equation (5) reduces to:

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[36] See: M.A. Adelman, "Comment on the 'H' Concentration Measure as a Numbers Equivalent," (1969) 51 Review of Economics and Statistics 99, for the seminal work in this area.

[37] L. Hannah and J. Kay, Concentration in Modern Industry, London: MacMillan (1977).

[38] J.E. Kwoka, "Large Firm Dominance and Price-Cost Margins in Manufacturing Industries," (1977) 44 Southern Economic Journal 183.

$$HKI = w\left(\frac{1}{N}\right)^{x} + y \sum_{i=1}^{N} (S_i - \overline{S})^{z} \qquad (7)$$

If one sets $w = x = y = 1$ and $z = 2$, the special case of the HHI emerges. The problematic issue is whether or not a "squaring" of the market shares assigns the appropriate weight. It would appear that these values for the parameters in equation (7) are chosen to construct an index which clearly and simply incorporates the two independent variables of number of firms and dispersion into the measure of concentration. As Kwoka queries:

> "While theory predicts the importance of both [number of firms and dispersion], the weights assigned to numbers and inequality by the Herfindahl are arbitrary, constrain the index within certain bounds, and imply trade-offs between these structural features in determining performance which should be derived and not assumed a priori."[39]

It would be interesting, although not within the scope of this research, to investigate the appropriate elasticity coefficient to be employed in the Canadian context. Perhaps, in Canada, due to the small market, one might envision an index which would apply less weight in the index to larger firms, allowing the attainment of minimum efficient scale. As Thomas J. Campbell, Director of the FTC's Bureau of Competition in the United States, replied to a query by AAG William F. Baxter on the use of the HHI in the U.S. merger guidelines:

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[39] See: Adelman, supra, n. 36.

> Now I heard the question, maybe improperly as: Why square it? Why not cube it? Why not raise it to the 1.7 power of the 2.2 power?" There I would have to say I have no answer to that. It would be a very nice empiric Ph.D. thesis, exploring the optimum exponent of market share variables. Squaring it is in the right general direction, but whether we might not do a great deal better by raising it to some power other than exactly 2.0 is a quite realistic possibility, an empiric question to which I have no answer.
>
> But I don't have much doubt about larger firms being more important in this kind of analysis, and that's what calls for some exponent greater than 1.0.[40]

For the purposes of this discussion, the HHI will be utilized as an acceptable first approximation.

The HHI is frequently referred to as the "numbers equivalent,"[41] being the number of equally sized firms necessary to generate that industry's HHI. The numbers equivalent is merely the inverse of the HHI:

$$NE = \frac{10,000}{HHI} \qquad (8)$$

This functional equality will be helpful _infra_ when comparing the HHI and the CR4.

E COMPARISON OF THE HHI AND CR4

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[40] The proof of this relationship is relatively straightforward. For equal market shares, HHI $= \Sigma S_i^2 = NS_i^2 = N(\frac{1}{N^2}) = \frac{1}{N}$. If market shares are expressed in terms of percentages, then NE = 10,000/HHI.

[41] "Panel Discussion: The New Merger Guidelines," (1982) 51 _Antitrust Law Journal_ 317, at p. 326.

The HHI cannot be mapped on a one-to-one basis with the CR4. In the 1984 version of the US Merger Guidelines, the Department of Justice makes reference to an empirical study which equates HHI levels of 1000 and 1800 to CR4 values of 50 percent and 70 percent respectively:

> The Department divides the spectrum of market concentration as measured by the HHI into three regions that can be broadly characterized as unconcentrated (HHI below 1000), moderately concentrated (HHI between 1000 and 1800) and highly concentrated (HHI above 1800). An empirical study by the Department [emphasis added] of the size dispersion of firms within markets indicates that the critical HHI thresholds at 1000 and 1800 correspond roughly to four-firm concentration ratios of 50 percent and 70 percent, respectively. Although the resulting regions provide a useful format for merger analysis, the numerical divisions suggest greater precision than is possible with the available economic tools and information. Other things being equal, cases falling just above and just below a threshold present comparable competitive concerns.[42]

Miller refers to this study in the following footnote:

> 1982 Guidelines, p.646. This empirical study is summarized in a memorandum dated February 19, 1982, from Lawrence J. White, director of the Economic Policy Office, to Tyler Baker, special assistant, "The Empirical 'Translation' Between Concentration Ratios and the Herfindahl Index." The analysis relates CR2 and CR4 to HHI for a random sample of 100 four-digit manufacturing industries for 1978. The specific translation of one measure into the other depends on the equation specified for the regression calculation. The relationship is apparently nonlinear.[43]

However, Miller indicates that a family or set of market share distributions and CR4 values exist for each value of HHI:

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[42] 1984 Merger Guidelines, 4490 CCH Trade Regulation Reporter, at 4493.10.

[43] Miller, supra, n. 34, at p. 612, footnote 27.

> As an exercise one can calculate various hypothetical distributions of S for firms in an industry to produce each of the two critical values of HHI in the 1982 Guidelines. Several examples for HHI of about 1,000 and 1,800 follow.
>
> | HHI | S_i | CR4 |
> |---|---|---|
> | 998 | 30, 1.4 (fify firms) | 34.2 |
> | 1,000 | 24, 16, 8, 2 (twenty-six firms) | 50 |
> | 1,004 | 20, 17, 12, 6, 3 (fifteen firms) | 55 |
> | 1,000 | 10 (ten firms) | 40 |
> | !,800 | 40, 3 1/3 (eighteen firms) | 50 |
> | 1,798 | 35, 18, 7, 5 (eight firms) | 65 |
> | 1,800 | 30, 20, 10 (five firms) | 70 |
> | 1,798 | 25, 22, 17, 14, 10, 10, 2 | 78 |
> | 1,810 | 19 (five firms), 1 (five firms) | 76 |
>
> One might note that HHI = 1,000 corresponds with a numbers equivalent of 10; HHI = 1,800, with NE = 5.56.[44]

Weinstock, in two well reasoned articles[45] expands on the difficulty of comparison and concludes that the CR4 levels cited in the Merger Guidelines appear to be the arithmetic averages of the 'range' of concentration levels. As Weinstock concludes in his 1984 article:

> As noted in the original article, a Herfindahl Index *cannot* be converted to a *single* four-firm concentration ratio; each HHI, in fact, relates to a *range* of CR4s. The HHI benchmarks of the guidelines at 1000 and 1800 convert to CR4s as shown in table 1. Thus, the CR4

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[44] *Ibid.*, 1984, at pp. 611-612.

[45] David S. Weinstock, "Using the Herfindahl Index to Measure Concentration," Summer (1982) 27 *The Antitrust Bulletin* 285; David S. Weinstock, "Some Little-Known Properties of the Herfindahl-Hirschman Index: Problems of Translation and Specification," (1984) 29 *The Antitrust Bulletin* 705.

values assigned to HHIs in the guidelines appear to be approximations of the arithmetic averages of the smallest and largest possible CR4s for each HHI. Although the CR4 figures quoted in the guidelines fall within the specified HHI ranges, they are misleading since they mask the fact that markets with significantly lower and higher CR$ values have the same Herfindahl Index.[44]

Table 1

CR4 Ranges for Guidelines' Herfindahl Benchmarks

Herfindahl Index	Minimum CR4 (%)	Maximum CR4 (%)	Mean (%)
1000	33.50	62.00	47.75
1800	44.73	84.48	64.61

F LIMITATIONS OF THE HERFINDAHL-HIRSCHMAN INDEX

Even though the pessimists would argue that the HHI is no more reliable than the familiar concentration ratio, most economists would be inclined to accept the HHI as a more comprehensive index. Notwithstanding this conditional preference, the HHI does not supercede the CR4 without several caveats. The most crucial parameter constraining an unfettered use of the HHI is the realization that market power is not invariably positively correlated with the index. Two fundamentally distinct schools have emerged as a result of the quest to theoretically link market power and the HHI. First, the Cournot model[47] assumes that each firm sets his output under the presumption that all other firms hold their respective outputs constant. From this simple assumption, Cournot derives two main conclusions:

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[44] Ibid., 1984, at p.707. See also: Appendix F, at pp. 716-717, for the complete mapping.

> First, for any industry, there exists a determinate and stable price- quantity equilibrium. Second, the equilibrium price depends upon the number of sellers. With a single seller, the monopoly price results. As the number of sellers increases, the equilibrium price declines until, when there are many firms, price approaches equality with marginal cost. Thus, the Cournot model indicates that competitive equilibrium is more closely approximated as the number of sellers increases - a prediction compatible with ordinary observation.[48]

However, as Irving Fisher observes:

> no business man assumes either that his rival's output or price will remain constant any more than a chess player assumes that his opponent will not interfere with his effort to capture a knight. On the contrary, his whole thought is to forecast what move the rival will make in response to his own.[49]

As Professor Kwoka has underscored:

> First, no explanation is offered as to why firms hold this particular conjecture regarding rivals' responses.

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[47] Augustin Cournot, Researches Into the Mathematical Principles of the Theory of Wealth, Homewood, Illinois: Irwin (1963).

[48] Scherer, supra, n. 18, at p. 152.

[49] Irving Fisher, "Cournot and Mathematical Economics," (1898) 12 Quarterly Journal of Economics 126; See also: Scherer, supra, n. 18, at p. 155, where he concludes "economists have come to believe that the Cournot assumption is quite unrealistic when applied to the pricing decisions involving only a few firms."

> That is, the theory does not derive this behavior as the result of some prior maximization problem, but simply postulates it. It clearly is not jointly profit maximizing for the firms....
>
> Secondly, the postulated behavior is not altogether plausible. The . . . Cournot model requires each firm to presume the continued absence of rivals' responses, despite repeated evidence that responses follow. The model in effect assumes no learning on the part of any firm. It is difficult to envision the real-world circumstances that would lead to such myopic behavior, and we must conclude that the Cournot model is itself weak, and correspondingly weak as a justification for the Herfindhal index.[50]

On the other hand, Stigler's model eliminates reaction functions.[51] He presupposes that oligopolists would like to collude to maximize joint profits subject to the constraint that transaction costs are not zero. Stigler treats the oligopoly as an expressed or implied cartel that is formed with full knowledge that resources will have to be used to detect cheating; although the policing scheme used will be imperfect, it will be tolerably effective. Stigler predicts that existing firms will not price in order to deter entry; rather, they will set a price, that maximizes the present value of their profit stream. As Stigler hypothesizes:

> The second theory, due to Stigler, is based on information (on price cuts) necessary to police a collusive agreement. "[Assume that] we wish concentration to measure likelihood of effective collusion. In the case of new customers [attracted by a secret price cut, M], for example, let the probability

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[50] J. Kwoka, "The Herfindahl Index in Theory and Practice." Unpublished manuscript.

[51] George J. Stigler, "A Theory of Oligopoly," (1984) 72 Journal of Political Economy 44.

> of attracting a customer be proportional to the firm's share of industry output (S_i). Then the variance of the firm's share of sales to new customers will be $M_N S_i(1-S_i)$, and the aggregate for the industry will be
>
> $$C = M_N \sum_{i=1}^{N} S_i(1+S_i)$$
>
> for N firms. This expression equals $M_N(1 - HHI)$, where
>
> $$HHI = \sum_{i=1}^{N} S_i^2$$
>
> is the Herfindahl [Hirschman] index of concentration.[52]

Although some empirical evidence exists to support Stigler's predictions, unfortunately as Kwoka emphasizes, the Stigler model is also based on unrealistic assumptions:

> [It] assumes perfect and costless information on the "origins and destinations of customers" . . . even while [the model] assumes the complete absence of information on rivals' prices. [Furthermore], the two derivations of the Herfindahl [which emerge from the Stigler model] are based on inconsistent assumptions, namely, whether or not firms pool information about a particular rival.[53]

One is left with the puzzling question whether or not there is a theoretical link between industrial structure and performance, and if so, what is the appropriate index to measure structure? The seminal work by Bain[54] correlated industrial concentration to profit rates; however, Bain's theory permitted practically any measure of industrial concentration to be suitable.[55] As Stigler notes:

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[52] Ibid., at p. 55.

[53] J. Kwoka, supra, n. 50.

[54] J.S. Bain, "Relation of Profit Rate to Industry Concentration: American Manufacturing, 1936-1940." (1951) 65 Quarterly Journal of Economics 293.

> Few theories of oligopoly provide any guidance in devising a measure of concentration. To be sure, this is largely due to the failure of theorists to derive such measures.[56]

In contrast, Demsetz rejected the structure - performance theory and the measurement of structure by the usual indices:

> No serious theoretical basis yet exists for this doctrine . . ., that monopoly [power] was significantly correlated with market concentration.[57]

As Miller notes:

> Thus, the mathematical proofs of the relationship between the HHI and the Lerner Index demonstrate at most a relationship that would exist only in markets that behave as no market is ever likely to behave. Accordingly, the proofs fail as arguments in support of the HHI as an optimal measure of real world monopolistic behavior.[58]

Consequently, because the theoretical justifications for monitoring market power with the use of structural indices are equivocal at best, one is diverted to empirical studies to ascertain whether any relevance and dependability should be afforded the structure - performance theory.

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[55] Leonard Weiss, "The Concentration Profits Relationship and Antitrust." Industrial Concentration: The New Learning edited by Goldschmid, Mann and Weston, Boston: Little, Brown & Co. (1974); Weiss lists hundreds of studies which study the structure-performance theory. In virtually all the empirical studies to that date, an empirical link existed.

[56] Supra, n. 50, at p. 31.

[57] Harold Demsetz, "Two Systems of Belief about Monopoly," Industrial Concentration: The New Learning, edited by Goldschmid, Mann and Weston, Boston: Little, Brown & Co. (1974) at p. 166.

[58] Supra, n. 34, at p. 487.

The literature on empirical studies does not definitively obviate the uncertainty and ambiguity; it is possible to find a study which would support any of the theoretical hypotheses. Several investigations found that price-cost margins were more closely correlated with the HHI than the CR4. Cowling and Waterson's[59] study of ninety-four British industries substantiated this view, as did Stigler's[60] extensive analysis and Rose and Fraser's[61] examination of the Texas banking industry.

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[59] Keith Cowling and Michael Waterson, "Price-Cost Margins and Market Structure." (1976) 43 Econometrica 267; See also: R.S. Khemani, Concentration in the Manufacturing Industries in Canada: Analysis of Post-War Changes, Research Monograph No. 8, Consumer and Corporate Affairs, Ottawa, Canada: Supply and Services, 1981. for a Canadian study of the factors which affect concentration. Khemani concludes that the significant concentration-increasing factors are firm multi-plant operations, horizontal mergers and firm exits. The significant concentration-decreasing factors are market growth and entry of new firms (p. 105). Khemani concludes that horizontal mergers are therefore not in the public interest. The difficulty with this analysis is the presumed positive correlation between concentration and market power.

[60] Supra, n. 51, at p. 58.

[61] Rose and Fraser, "The Relationship Between Stability and Change in Market Structure: An Analysis of Bank Prices." (1976) 24 Journal of Industrial Economics 251.

Two studies have produced neutral results: Scott's[62] analysis found no difference between HHI and CR3 and Short's[63] study found the HHI and CR to be equal predictors.

Four studies have found the HHI to be an inferior estimator of market power. The Jones, Laudadio and Percy[64] research, a Canadian study, found the HHI significantly less accurate than the CR4; Hannan[65] likewise found the HHI less dependable, as did Weiss.[66] Finally, Kwoka[67] found that the CR2 outperformed the CR4 and HHI. Kwoka reasons that this result is compatible with the existence of "procompetitive rivalry from a sufficiently large mid-ranked firm."[68] Assistant Attorney General Baxter dismissed Kwoka's finds as not very persuasive.[69]

It appears patently obvious to the informed student that the economic literature leaves unsettled and unresolved the structure - performance paradox. Neither the question of the causal link between industrial structure and market performance nor the choice of the optimal concentration measure have been satisfactorily answered. As Kilpatrick notes, "the particular choice is not crucial"[70] in choosing amongst the available structural measures. Cohen and Sullivan echo this view:

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[62] Scott, "Homogenizing Deconcentration: Estimation and Simulation." (1980) 62 Review of Economics and Statistics 612.

[63] Short, "The Relationship between Commercial Bank Profit Rates and Banking Concentration in Canada, Western Europe and Japan." (1979) 3 Journal of Banking and Finance 209.

[64] Jones, Laudadio and Percy, "Market Sturcture and Profitability in Canadian Manufacturing Industry: Some Cross-Section Results." (1973) 6 Canadian Journal of Economics 356.

[65] Hannan, "Limit Pricing and the Banking Industry." (1979) 11 Journal of Money, Credit and Banking 438.

[66] L. Weiss, "Quantitative Studies of Industrial Organization." (1970) Frontiers of Quantitative Economics (1970) 302.

[67] Supra, n. 38.

[68] Ibid., at p. 28.

[69] Supra, n. 41, at p. 333.

> In summary, there is little empirical support for the HHI as a measure of the competitiveness in an industry. Even assuming that the methodology of the studies is valid, the studies taken as a whole would not lead an unbiased observer to conclude that the HHI generally outperforms other indices.[71]

Miller, succintly summarizing the debate in the following passage, concludes that the HHI is not inferior to any other measure of concentration:

> In several articles John Kwoka, Jr., has investigated numerous indices of structure: the individual firm shares (S for each of the largest firm shares), HHI, CR4, and CRN for N = 1, 2, . . . , 10. He concludes that the choice of a concentration ratio (CRN) does matter; the relationship among the performance variable (a PCM) and CRN and S_i (for i = 1, . . . , 4) is strongest for CR2 and for S_1, S_2, and S_3, and declines for more inclusive CRNs; apparently it is the market shares of the largest two or three firms which influence performance. In a direct comparison of CR4 and HHI (both produced statistically significant results), there was little to choose. Kwoka's conclusion expresses economists' current empirical

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[70] Robert W. Kilpatrick, "The Choice Among Alternative Measures of Industry Concentration." (1967) 49 Review of Economics and Statistics 258.

[71] Supra, n. 4, at p. 492.

> knowledge of the relative importance of HHI: the results were so similar that they "provide little support for the alleged superiority of the HHI index." Nor is HHI inferior, either.[72]

In policy analysis, the paucity of theoretical justification for the use of the HHI as a structural indicator of the probability of market power has been posited as the major shortcoming for use of the index. However, if the structural - performance paradigm is accepted, then the HHI is as effective a measure as the alternatives. Furthermore, any reticence to employ a structural test to determine the merits of a merger at trial is mitigated if the test is merely employed as a prima facie guideline for the purpose of shepherding the administration through injunctive procedures.

A second disadvantage of the HHI is illustrated by Cohen and Sullivan by way of hypothetical market structures. They simulate markets which would be enjoined under CR-thresholds and not HHI-thresholds. They conclude:

> Thus, even an index with the touted advantages of the HHI - its summary nature and disproportionate weight given to larger firms - can produce prosecutorial decisions that differ from those suggested by the HHI.
>
> This phenomenon - different measures of concentration producing prosecutorial decisions that differ from those suggested by the HHI for any given benchmark - is more than just a theoretical possibility. It can occur whenever the HHI of a market is near a benchmark. Accordingly, the validity of the

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[72] Supra, n. 34, at p. 609.

> HHI formula must be exmined before the validity of the relative concentrations generated by that formula can be evaluated.[73]

However, this proposed shortcoming is applicable to any measure of concentration chosen.

A third major criticism of the HHI eminates from its summary nature; to calculate the index precisely, statistical data must be available for all firms' market shares. In an injunctive proceeding, this could create an insurmountable obstacle. This requirement did not escape the notice of Miller:

> It is important to note that the data requirements for measuring HHI in an actual market are severe. Not only must each individual firm's contribution to the market be measured, rather than the contributions of the largest four or eight firms, but those contributions must be relative to all firms' contributions, that is, relative to the entire market. The calculation of HHI thus requires (a) the delineation of the market, with all the calculations and judgments about cross-elasticities of supply and demand, and (b) the participation by individual firms in that market. In no way does the calculation of HHI avoid the problem of determining what the market is, in both the geographic and product dimensions. These difficulties are well known in antitrust, and what a court accepts as "the" market may - as in the

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[73] Supra, n. 4, at p. 500.

Cellophane case - actually determine the decision.[74]

Fortunately, in a widely dispersed market, the omission of the market shares of the insignificant fringe will not alter the value of the HHI appreciably. As a practical result, if data is available for the market shares of the major players in the industry, data which would be necessary in any event to calculate the CRN, then it is possible to overcome this empirical restriction.[75]

Weinstock, in his first article examining the HHI, warns that any merger test that incorporates an increase in the HHI as a variable in merger acceptability must view the HHI relative to the initial concentration levels in the market:

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[74] Supra, n. 34, at p. 596; See also: Weinstock, supra, n. 45, at p. 287: One problem from which all measures of concentration suffer - including both the CRN analysis and the Herfindahl Index - is that in order to be meaningful they require that the market be defined, i.e., both the product and geographic markets must be delineated. In addition, the time factor must be taken into account since changing conditions - e.g., technological innovation, availability of substitute products, reduced barriers to entry, etc. - may precipitate the deconcentration of a market. Another factor that must be considered is the extent to which there are barriers to entry into the market. The Herfindahl Index, like other measures of concentration, is only one part of an analysis of a market. Obviously, these and other factors must also be taken into account.

[75] See: Weinstock, Ibid.: "The fact that the smaller firms' shares are weighted less than those of the larger companies allows a Herfindahl analysis to be utilized even if 100% of the market is not included. However, the accuracy of this measure of concentration is, of course, affected if any data are omitted."
See also: Cohen and Sullivan, supra, n. 4, at p. 477: "Unavailability of data concerning the market share of very small firms is rarely a significant problem when using the HHI."

> [M]ergers in less concentrated markets may be open to concern under the Herfindahl analysis more frequently than mergers in more concentrated markets.[76]

Secondly, Weinstock points out that the numbers equivalent, NE, sets the lowest possible level of HHI. Consequently, industries which may have a small number of members for efficiency reasons may automatically surpass any given HHI-threshold.[77] In his most recent study, Weinstock re-emphasizes that the HHI translates into a range of concentration ratios.[78]

Further study is desirable to develop an index that accounts for the following variables which impact on concentration:

(a) the relative influence of geographic market segmentation,

(b) International trade,

(c) Multi-plant operations, and

(d) Barriers to entry.

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[76] Supra, n. 45, at 289.

[77] For example, in the 1984 U.S. Merger Guidelines, a market with less than ten members would breach the "moderately concentrated" threshold of HHI = 1000, and a market of less than six firms would surpass the "highly concentrated" threshold of 1800.

[78] Supra, n. 45, at p. 707.

In the light of these constraints attending the use of the HHI to monitor and predict market power, one must balance the potential advantages of this summary index.

G ADVANTAGES OF THE HERFINDAHL-HIRSCHMAN INDEX

The elevation of the HHI to its present level of supremacy in American antitrust policy may be owed to Posner's[77] initial reference to the index in 1969. More recently, the index has been referenced in Areeda and Turner's influential treatise:

> 913c2. Which concentration measure? As we explained in b, the Herfindahl index, though inferior to simple aggregate shares, seemed superior to concentration ratios as a general test of mergers. Though the choice is closer, the Herfindahl index also seems superior as a basis for varying presumptively unlawful aggregate shares. It is responsive to large size disparities among leading firms - though perhaps overly so - and to the number and size of the remaining firms. Concentration ratios are wholly insensitive to each, though each affects the probability and magnitude of non-competitive pricing. Consequently, a single specific Herfindahl index seems more likely than a concentration ratio to comprehend an array of varying market structures with comparable performance probabilities. And for that reason, use of the Herfindahl index would reduce the arbitrariness of a single threshold and thus the need for a more complicated approach.[88]

The "Informal Task Force," comprised of a distinguished group of lawyers also preferred the use of the HHI.[11] As a result of these recommendations, the 1982 U.S. Merger Guidelines shifted from the use of the CR4 to the HHI as the preliminary structural test in evaluating potentially harmful mergers. In addition, in the American jurisprudence, judicial interest in the HHI had been expressed in several cases.[12] This tack, as adopted by the 1984 Merger Guidelines, was substantiated as follows:

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[77] R.A. Posner, "Oligopoly and the Antitrust Laws: A Suggested Approach." (1969) 21 Stanford Law Review 1562.

[88] Phillip Areeda and D.F. Turner. Antitrust Law. Boston: Little, Brown & Co, (1980).

> [10] 3.1 Concentration and Market Shares.
>
> Market concentration is a function of the number of firms in a market and their respective market shares.[13] Other things being equal, concentration affects the likelihood that one firm, or a small group of firms could successfully exercise market power. The smaller the percentage of total supply that a firm controls, the more severely it must restrict its own output in order to produce a given price increase, and the less likely it is that an output restriction will be profitable. If collective action is necessary, an additional constraint applies. As the number of firms necessary to control a given percentage of total supply increases, the difficulties and costs of reaching and enforcing consensus with respect to the control of that supply also increase.
>
> As an aid to the interpretation of market data, the Department will use the Herfindhal- Hirschman Index ("HHI") of market concentration. The HHI is calculated by summing the squartes of the individual market shares of all the firms included in the market under the standards in Section 2 of these guidelines.[14] Unlike the traditional four-firm concentration ratio, the HHI reflects both the distribution of the market shares of

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[11] Joffe, Edwards, et al., "Proposed Revisions of the Justice Department's Merger Guidelines." (1981) 81 Columbia Law Review 1543, at p. 1561.

[12] In the Matter of Lotton Industries, Inc., 530 F.Supp. 315 (N.D. Ohio 1981), aff'd, 669 F.2d 378 (6th Cir. 1981); United States v. Black and Decker Manufacturing Co., 430 F.Supp. 724 (D.Md. 1976).

> the top four firms and the composition of the market outside the top four firms. It also gives proportionately greater weight to the market shares of the larger firms, which probably accords with their relative importance in any collusive interaction.
>
> [13] Markets can range from atomistic, where very large numbers of firms that are small relative to the overall size of the market compete with one another, to monopolistic, where one firm controls the entire market. Far more common, and more difficult analytically, is the large middle range of instances where a relatively small number of firms account for most of the sales in the market.
>
> [14] For example, a market consisting of four firms with market shares of 30 percent. 30 percent, 20 percent and 20 percent has an HHI of 2600 ($30^2 + 30^2 + 20^2 + 20^2 = 2600$). The HHI ranges from 10,000 (in the case of a pure monoply) to a number approaching zero (in the case of an atomistic market). Although it is desirable to include all firms in the calculation, lack of information about small fringe firms is not critical because such firms do not affect the HHI significantly.[83]

The HHI includes two vital elements of information which are omitted in the discrete concentration ratio. As mentioned previously, the degree of equality in firm size and the number of member firms which comprise the market. A decrease in either of these independent variables will impact directly on the anticipated level of market power. If the HHI index were to be employed as a "guideline" to assist the Director in determining the appropriateness of instituting injunctive proceedings respecting a proposed or consummated merger, several positive advantages would emerge. First, the Bureau of Competition Policy would not be sidetracked by weighing and ranking the myriad of possible behavioural variables which might or might not impact on the potential for collusive conduct. Second, a degree of certainty and predictability would be available to the general business community. Third, the Director need not be compelled to evaluate the conduct and performance of the merging firms; this responsibility should be vested in the courts or Tribunal. Moreover, the Director is simply estimating the economic impact of the transaction, not the socio-political incidence. Finally, of pragmatic significance, is the cost-efficient use of government (taxpayer) resources which would materialize with the adoption of this relatively simple structural test, in contradistinction to a more comprehensive and complex behavioural or performance approach. In fairness, it must be highlighted that the HHI is being recommended for use by the Director at the institution stage only, not to replace the statutory tests enacted in sections 72 and 76 Competition Act, which would be operative in proceedings before the Competition Tribunal and possibly the courts. As Weinstock concludes:

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[83] 1984 Merger Guidelines, CCH Trade Regulation Reporter, 4493.10

> Despite the fact that the Herfindahl Index requires individual company data for each of the firms in a market - information which may be difficult to obtain - and utilizes mathematical computations that are more complicated than those needed in a CR analysis,

nevertheless it gives a more complete picture of the market because of its ability to include all of the firms in a market and to weight each according to its relative size.[66]

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[66] Supra, n. 45, at p. 296.

IX THE 1984 U.S. MERGER GUIDELINES

A INTRODUCTION

The United States has utilized merger guidelines since 1968[1] to escort the Department of Justice[2] (DOJ) through its administrative decision-making procedures respecting section 7 Clayton Act[3] proceedings. At the outset, the major distinction between the U.S. merger guidelines and the present proposal must be highlighted. The U.S. merger guidelines are intended as a preliminary simulation of the relevant factors which may emerge in an action under the substantive merger proscriptions; the recommendations in this discussion are contemplated in the context of an objective checklist to assist the Director in the determination of possible injunctive proceedings. This restriction to temporary relief is justified on two grounds. First, it is suspected that the operative and effectual provisions of the Competition Act will be the preliminary and interlocutory injunctive sections;[4] second, tailoring the guidelines to the substantive merger provisions of the Competition Act would submerge the Director in the quagmire of evaluating efficiency and failing company defences, net advantages, likelihoods, redistributions, to list but a few. The contentious issue, which will become apparent after a review of the U.S. guidelines, is the degree to which "other factors" should be included in the guidelines to clarify and buttress the simple structural HHI test. As a general proposition, the Canadian guidelines for injunctive relief need not be as complex and extensive as their American parent. In addition, serious concern must be directed towards deleting some of the exemptions and defences, streamlining the checklist, and relegating these "other factors" to adjudication by the Tribunal on subsequent application by the Director.

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[1] References to the three American DOJ Merger Guidelines will be as follows:
(a) 1968 Merger Guidelines, CCH Trade Regulation Reports, par. 4510.
(b) 1982 Merger Guidelines, CCH Trade Regulation Reports, par. 4500.
(c) 1984 Merger Guidelines, CCH Trade Regulation Reports, par. 4490.

[2] The Department of Justice in the U.S. is the counterpart of the Director in Canada.

[3] Clayton Act, Act of October 15, 1914, C. 323; 38 Stat. 730, as am. by The Celler-Kefauver Act, s.7.

The 1984 Merger Guidelines are a comprehensive framework assimilating and molding the amorphous mass of current thinking on merger policy into an integrated and systemized game plan. The 1984 Guidelines stress the horizontal effects of mergers, both in terms of horizontal mergers per se, and with respect to the horizontal effects of non-horizontal mergers (vertical and conglomerate mergers).[5] In both cases, the DOJ will focus on the following five steps:

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[4] Competition Act, S.C. 1986, formerly Bill C-91, sections 72 and 76 respectively.

1. The Delineation of the Relevant Market,
2. The Calculation of Market Shares,
3. The Preliminary Decision Rules,
4. Other Factors, and
5. Defences.

Many commentators surmise that the determination of the market is subordinate, even non-essential, in the non-horizontal merger case; nonetheless, to deduce that the merging parties' markets do not intersect requires an antecedent determination of the relevant market. Additionally, the specifically identified concerns of potential competition, foreclosure and collusion in the 1984 Guidelines all require a recognition of the pertinent market under scrutiny.

The following analysis segments the inquiry into horizontal and non-horizontal mergers, as well as outlines the five steps enumerated above. Significant import is placed on the development of the relevant market delineation. The final section investigates the modifications which will be necessary in order to adopt a similar procedural mechanism for injunctive relief in the

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[5] Note that in the 1968 version of the Guidelines, greater emphasis was placed on conglomerate mergers as a separate concern (Section III, para. 17).

Canadian setting.

B THE RELEVANT MARKET

1. The Theoretical Foundations of the Relevant Market Determination

(a) The Theoretical Underpinnings of Market Delineation

On June 14, two years to the day after the DOJ issued the 1982 Merger Guidelines, the 1984 Merger Guidelines were issued to refine and clarify the original framework. As the DOJ Statement which accompanied the Guidelines claimed:

> Although the revisions make some important refinements and clarifications, the Department believes that the 1982 Merger Guidelines provide a sound framework for applying the antitrust laws to mergers and do not require extensive modification.[6]

As mentioned above, the Guidelines are an administrative tool to be used at the pre-trial stage:

> The Guidelines are designed primarily to indicate when the Department is likely to challenge mergers, not how it will conduct the litigation of cases that it decides to bring. Although relevant in the latter context, the factors contemplated in the standards do not exhaust the range of evidence that the Department may introduce in court.[7]

In order to appreciate the thrust of the Guidelines, a clear understanding of the evil for which they were created to detect must be realized. The seminal work in this area was accomplished in 1981 by Landes and Posner[6] in their inspiring article entitled "Market Power in Antitrust Cases." Landes and Posner define "market power" to be:

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[6] 1984 Merger Guidelines, supra, n. 1, at 4490.

[7] Ibid., at 4491.

> the ability of a firm (or a group of firms acting jointly) to raise price above the competitive level without losing so many sales so rapidly that the price increase is unprofitable and must be rescinded.[7]

The misconduct alluded to above and which antitrust policy should attempt to prevent is "market power." As the Guidelines emphasize:

> The unifying theme of the Guidelines is that mergers should not be permitted to create or enhance "market power" or to facilitate its exercise. A sole seller (a "monopolist") of a product with no good substitutes can maintain a selling price that is above the level that would prevail if the market were competitive. Where only a few firms account for most of the sales of a product, those firms can in some circumstances either explicitly or implicitly coordinate their actions in order to approximate the performance of a monopolist. This ability of one of more firms profitably to maintain prices above competitive levels for a significant period of time is termed "market power". Sellers with market power also may eliminate rivalry on variables other than price. In either case, the result is a transfer of wealth from buyers to sellers and a misallocation of resources.
>
> "Market power" also encompasses the ability of a single buyer or group of buyers to depress the price paid for a product to a level that is below the competitive price. The exercise of market power by buyers has wealth transfer and resource misallocation effects analogous to those associated with the exercise

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[6] W. Landes and R. Posner. "Market Power in Antitrust Cases." (1981) 44 Harvard Law Review 937.

[7] Ibid., at p. 937.

of market power by sellers.[10]

The similarity between the definition proposed by Landes and Posner and embraced by the DOJ is striking. Accepting the premise that the target of antitrust legislation is to prevent market power, the guidelines must balance two conflicting goals. On the one hand, the DOJ recognizes that most mergers do not threaten competition and that some are actually procompetitive; on the other hand, the only effective means of regulating harmful mergers is to intercede in the incipiency. As the preamble to the Guidelines concludes:

> Although they sometimes harm competition, mergers generally play an important role in a free enterprise economy. They can penalize ineffective management and facilitate the efficient flow of investment capital and the redeployment of existing productive assets. While challenging competitively harmful mergers, the Department seeks to avoid unnecessary interference with that larger universe of mergers that are either competitively beneficial or neutral. In attempting to mediate between these dual concerns, however, the Guidelines reflect the congressional intent that merger enforcement should interdict competitive problems in their incipiency.[11]

Market power is defined as the price-cost margin (PCM), or monopoly overcharge, and is conventionally measured by the Lerner Index:[12]

$$L = \frac{P-MC}{P} ,$$

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[10] 1984 Merger Guidelines, *supra*, n. 1, at 4491.

[11] 1984 Merger Guidelines, *supra*, n. 1, at 4491.

[12] Lerner. "The Concept of Monopoly and the Measure of Monopoly Power." (1934) 1 *Review of Economic Studies* 157, at p. 169.

(1)

where P - monopoly price

MC - marginal cost at monopoly output

Qm.

As Landes and Posner remark, the Lerner Index is inversely related to the ith firm elasticity of demand,[13] η_i^D:

$$L = \frac{1}{\eta_i^D} \qquad (2)$$

If quantitative estimates of either MC or η_i^D were readily ascertainable, then the calculation of the effect of a merger on market power would be perfunctory. Unfortunately, these variables are seldom available. This empirical stricture is discerned by the authors:

> While at first glance equation (1) [equation (2) supra] appears to offer a shortcut to the determination of market power in an antitrust case, its crucial dependence on the firm's elasticity of demand makes its utility, as we shall see, primarily conceptual.[14]

Apart from the hurdle of estimating firm elasticity of demand, L will always tend to overstate the monopoly overcharge. The Lerner Index will operate as a "ceiling" estimate of market power by reason of its equality to the larger PCM (price-cost margin) rather than the smaller, but more accurate, margin by which monopoly price exceeds the corresponding competitive price. Finally, if the monopolist is a price discriminator, the firm will face several L-index levels.[15] Notwithstanding these caveats, if the estimation of firm elasticity of demand were possible, the Lerner index could be employed to monitor the harmful effects of mergers. Landes and Posner proceed to pose the question whether market shares (and consequently the HHI) could be used as a "second best" alternative for the purpose of reflecting the level of market power.

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[13] Supra, n. 8, at p. 940. The proof of this equation can be found in Appendix E.

[14] Supra, n. 8, at p. 943.

Landes and Posner resurrect the mathematical relationship between firm elasticity η_i^D, market elasticity η_m^D, fringe firm elasticity of supply η_i^S, and the market share for firm i, S_i. The extremely influential and concise relationship[16] which appears to have shaped the Guidelines follows:

$$\eta_i^D = \frac{\eta_m^D}{S_i} + \frac{\eta_i^S(1 - S_i)}{S_i} \qquad (3)$$

From this relationship, one may derive generally predictable causal links between market power and the three independent variables, η_m^D, η_j^S and S_i. Market power varies:

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[15] See: 1984 Merger Guidelines at 4492.103 for the practical application of this observation. As an aside, one must recall that the monopolist will not produce at an output level which corresponds to $\eta_i^D < 1$.

[16] See: Appendix E for the mathematical derivation of this equation (3).

(a) INDIRECTLY with η_m^D;

The higher the market elasticity of demand, the greater the availability of good substitutes and the lower the incumbent's ability to sustain price above the competitive level.

(b) INDIRECTLY with η_j^S;

The greater the value of the fringe firm's or new entrant's ability to expand production in response to a price increase in the relevant market, the less will be the market power of the aspiring monopolist.[17]

(c) DIRECTLY with S_i;

The greater the market share of incumbent firm i, the greater the potential for firm i to exhibit the conventional characteristics of the "dominant" firm.[18]

It also becomes apparent from a review of equation (3) that the product and geographic markets influence the extent of market power; furthermore, the effect of the relevant market may be segmented into a dependent two-stage procedure.

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[17] Note: Theoretically, even though firm i may control one hundred percent of the market, firm i may have no market power if $\eta_i^S = \infty$.

[18] Note: As discussed *supra* at some length, the theory of collusion is secondary in the analysis proposed by Landes and Posner.

First, if one sets the fringe elasticity of supply to zero, equation (3) reduces to

$$\eta_i^D = \frac{\eta_m^D}{S_i} \qquad (4)$$

Assuming the product market has been established, the value of will be determinable and the inverse relationship between market share and firm elasticity obvious. Two reservactions must be expressed regarding equation (4). First, the product must be defined before the effect of market share on market power can be ascertained. Second, the market power resulting from equation (4) is the "upper bound" on the monopoly overcharge; such market power will inevitably be restricted by the circumscription of the geographic market.

Turning to the influence of the geographic market on market power, assuming $\eta_m^D = 0$, equation (3) reduces to:

$$\eta_i^D = \frac{\eta_j^S}{S_i} - \eta_j^S \text{ , where } \eta_j^S > 0 \qquad (5)$$

As predicted, an inverse relationship exists between η_i^D and S_i, the market share of firm i. In addition, equation (5) indicates that the effect of supply substitution by peripheral firms is crucial for the intermediate step of delineating the relevant geographic market and ultimatly resolving the degree of market power.[17] The degree of supply substitutability of the fringe community will vary directly with the market share and supply elasticity of these producers. Consequently, the impact of fringe suppliers on the curtailment of market power cannot be overlooked. As Landes and Posner conclude:

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[17] Supply substitution will be essential in the determination of the relevant product market as well as the relevant geographic market in the 1984 Guidelines.

> The smaller the market share of the competitive fringe, the smaller the increase in output of the fringe will be for any price increase (holding constant the fringe supply elasticity). Likewise, the smaller the increase in fringe output for a given price increase, the smaller will be the reduction in firm i's output necessary to bring about that increase. Hence the demand elasticity for firm i will be lower the smaller the market share of the competitive fringe is. Intuitively, it is cheaper to raise price by curtailing output if fringe sellers have a lower market share since the same percentage increase by the fringe will yield a small absolute increase in their output.[30]

(b) Adjusting Market Share to Infer Market Power

As Landes and Posner are well aware, the only relatively exact figures which will likely be available to ascertain market power are market share figures:

> 2. Adjusting Market Share to Infer Market Power. - Assuming the only "hard" number in an antitrust case is likely to be the market share, is there still some way to use the basic approach illustrated by Table I?[31]

Landes and Posner propose two alternate approaches for the use of market share statistics to infer market power. One method would accept the preliminary values for market share, but modify their significance with reference to the additional factors which conjunctively affect market power:

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[30] Supra, n. 8, at p. 947.
[31] Ibid., at p. 958.

> One possibility is not to define market power in terms of specific market shares at all, but instead to _interpret_ the market share statistics in each case by reference to qualitative indicia of the market elasticity of demand and the supply elasticity of the fringe firms. If either the market elasticity of demand or the elasticity of supply were high (although no precise numbers could be attached to them), different inferences would be drawn from the defendant's market share than if either or both of these elasticities were low.[22]

The second technique would adjust _a priori_ the market to account for these relevant parameters, then calculate the amended market shares:

> Another possible approach to determining market power when elasticities are unknown is to use "guesstimates" of elasticities in defining the market in the first place. Here the adjustment for elasticities comes not after a market share is calculated but when the market is defined. This approach, illustrated in some of the examples in Part I, is further illustrated in our discussion of the definition of the geographical market below. It is in fact the dominant judicial method of taking account of elasticities of demand and supply.[23]

Neither approach embodies any inherent conceptual advantage; however, the second approach has been the procedure most widely applied in both the American and Canadian jurisprudence, not to mention the 1984 Merger Guidelines. As well, a preliminary adjustment to the pertinent market would focus the adjudicative body on the relevant issues of demand

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[22] _Ibid._

[23] _Ibid._, at p. 960.

and supply substitutability. The Canadian courts have been sorrily remiss in their attention to these issues. As a consequence, it is recommended that the approach instituted in the American guidelines be employed in a set of Canadian pre-merger administrative guidelines for injunctive relief.

(c) The Relevant Product Market

Landes and Posner postulate that the relevant product market should be defined having regard to both the substitution in consumption and production. Respecting demand elasticities, if the firm elasticity of demand were known, market power could be measured directly by employing equation (2). Unfortunately, η_i^D is seldom available. Although the authors do not explicitly state this relationship, the general tenor of the article suggests that the provisional market should be expanded as market elasticity of demand increases. As the authors conjecture:

> If the market were defined broadly - that is, if distant as well as close substitutes for firm i's product were included in the market - i's market share would tend to be small, but the market elasticity of demand would also tend to be low; so many substitutes would be included in the market that consumers would have difficulty substituting away from the market if market price rose. Hence a smaller number would be divided by a smaller number in the first term on the right-hand side of equation (2) [equation (3) in this paper]. If instead the market were defined narrowly, the firm's market share would be larger but the effect on market power would be offset by the higher market elasticity of demand; when fewer substitutes are included in the market, substitution of products

outside of the market is easier.[24]

Similarly, on the supply side, an increase or relatively high η_j^S should be used to interpret the provisional market in a broad context and expand it accordingly:

> Similar considerations come into play when we look at the market from the standpoint of substitution in production. If the market is defined without regard to the possibility of entry into the market by firms not now making the same product as firm i, then the market share of the competitive fringe will tend to be low but the elasticity of supply will tend to be high. This is because a slight price increase will not only stimulate additional production by the fringe, but also attract into the market any firm that can readily substitute this product for its current output. Conversely, defining the market broadly to include producers of different products who could and would make the product in question if its price rose even slightly will yield a higher market share for the competitive fringe but a lower elasticity of supply, again producing offsetting effects in equation (2). A price increase will now have a smaller effect in bringing in production from firms outside the market - the market is already defined to include those firms.[25]

The authors warn that the supply substitution is circumscribed by the degree of demand substitution to some extent. As they note:

> Therefore, the courts should include in the market the output of products that are good substitutes in production but not in consumption only if the included manufacturers are capable to producing something like the full range of products included in the product market as originally defined.[26]

In summation to this point, the provisional product market should be expanded if the market elasticity of demand and the fringe firm elasticity of supply are high. As alluded to in Landes and Posner's article:

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[24] Ibid., at p. 962.
[25] Ibid., at p. 963.
[26] Ibid., at p. 947.

> In fact, if market share alone is used to infer power, the market share measure in equation (2) [equation 3, supra], which is determined without regard to market demand or supply elasticity (separate factors in the equation), will be the wrong measure. The proper measure will attempt to capture the influence of market demand and supply elasticity on market power.[27]

A third factor which the authors address at length but do not appear to incorporate into a policy formula is the effect of the absolute size of the market itself on market power. A model is constructed under the following assumptions which relates the absolute market size to the relative market share, S_i, in order to maintain a constant level of market power:

(a) Deadweight social loss is the only social cost considered,

(b) Demand is linear,

(c) Marginal costs are constant,

(d) $\eta_j^S = 0$, and

(e) Deadweight social loss of $24.5 million is the requisite threshold of market power to warrant antitrust prosecution.[28]

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[27] Ibid., at p. 947.

As a result of the application of the equation found in footnote 28 of this text, the authors develop Table I infra, a study of which implies that for a given level of deadweight social loss and a constant η_m^D, as the absolute market size increases a smaller market share is required to maintain the same market power.

TABLE I

Market Share Variations

	P x Q (millions of dollars)			
	\$100	\$200	\$500	\$1000
1	.70	.49	.31	.22
1.5	.86	.61	.38	.27
2	.99	.70	.44	.31

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[28] Deadweight social loss (dwsl) is the amount of consumer surplus lost as a result of an increase in price from the competitive level. In general, dwsl equals:

$$\text{dwsl} = \int_{Qm}^{Qc} P dQ - \int_{Qm}^{Qc} MC\, dQ \ .$$

Given the assumptions in the Landes-Posner model, dwsl may be derived by use of the following equation:

$$\text{dwsl} = S_i^2 . P \times \frac{Q}{2\eta_m^D} \ .$$

See: Landes & Posner, at p. 954, footnote 32 for the derivation of the above equation.

Note: Deadweight loss is constant at $24.5 million.[29]

As the authors conclude:

> The main point of Table I is the arbitrariness of basing judgments of legality on market share figures evaluated independently of the size of the market. If very high market shares are required to justify a finding of monopoly power in a small market, then a lower share should suffice in a large market. Conversely, if a very high market share is required for a finding of monopoly power in a large market, then in a small market a finding of monopoly power might never be appropriate.[30]

The rationale suggested for this startling observation may be embedded in the premise that the remainder of the industry is highly fragmented:

> The first factor, which is usually neglected, is relevant because the actual economic injury caused to society is a function of not only the deviation between price and marginal cost but also the amount of economic activity over which the deviation occurs. If the amount of activity is small, the total social loss is small, and an antitrust proceeding is unlikely to be socially cost justified; this is especially true when the remedy sought (such as divestiture) involves heavy administrative and disincentive costs even in cases where the stakes to the parties are relatively modest.[31]

The policy implication of this discovery is to suggest that only major or leading sectors in the economy should be under antitrust merger scutiny. In the Canadian context, only large mergers in dominant sectors of the economy need be subject to substantive proscriptions.[32] Mergers in sectors which are new, growing and not entrenched may be of little concern with respect to their impact on social costs.

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[29] Supra, n. 8, at 955. If firm i has a market share S = 70% and output (sales) of $800 million, when = 1, the dwsl resulting will be $24.5 million.

[30] Ibid.

[31] Ibid. at p. 953.

The final variable which is proposed as an element to interpret the market delineation is the cross-elasticity of demand.[33] In the *Cellophane* case,[34] the court found that flexible wrapping papers were a good substitute for cellophane on account of evidence of a high cross-elasticity. The fallacy with this reasoning lies in the fact that, if the price is set high enough, many goods will be transformed from poor to good substitutes. Merely by studying the definition of cross-elasticity, a drop in the price in the denominator will yield an increase in the value of η^{D}_{kx}. It must also be recalled that cross-elasticity measures potential demand substitutability; market delineation solely on the basis of η^{D}_{kx} omits the entire

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[32] This concept may have precipitated the amendments to the 1984 Guidelines by the inclusion of section 3.21.

[33] Cross elasticity of demand, , is the relative change in the quantity demanded for good k due to change in the price of good x. A high cross-elasticity implies, at the current price level, the products are good substitutes. Mathematically:

$$\eta^{D}_{kx} = \frac{\Delta Q_k / Q_k}{\Delta P_x / P_x} .$$

[34] *U.S.* v. *E.I. due Pont de Nemours and Co. et al.*, 351 U.S. 377 (1956); See: Peter Asch, *Industrial Organization and Antitrust Policy*, Toronto: Wiley & Sons, 1983, at p. 247 for a discussion of this case. See also: *U.S.* v. *Aluminum Co. of America*, 148 F. 2d 416 (1945), for a discussion of the opposite situation where the price is maintained at a *low* level.

concept of substitution in production. Although cross-elasticity may be a determinant of firm elasticity of demand,[35] firm elasticity is the proportion weighted average of the cross-elasticities between good x and *all* other goods. Consequently, unless data on the proportional share of income spent on good x relative to all other goods is available, and the corresponding cross-elasticities for each potential substitute can be estimated at the current price of the investigated product, cross-elasticity will not operate as a dependable barometer of market power.[36] Of interest, a high cross-elasticity may simply imply a firm elasticity greater than unity, which is always the case for a monopolist producing in the region where elasticity of demand is elastic. Landes and Posner concede:

> Because every monopolist faces an elastic demand ($\epsilon_i^d > 1$) at its profit-maximizing output and price, there is bound to be some substitution of other products for its own when it is maximizing profits, even if it has great market power. If the Court's reference to the "high" cross-elasticity of demand between cellophane and

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[35] Mathematically,

$$\eta_x^D = \sum_{k=1}^{n} \left(\frac{\alpha_k}{\alpha_x}\right) \eta_{kx}^D ,$$

where η_x^D - firm elasticity of demand

η_{kx}^D - cross-elasticity of good k due to change in price of x

α_k, α_x - share of products k and x in income. See also: J. Henderson and R. Quandt. *Microeconomic Theory*. (3d) New York: MacGraw-Hill (1980) at p. 33; J.P. Gould and C.E. Ferguson. *Microeconomic Theory*. Homewood, Illinois: Irwin, (1980), at p. 66.

[36] *Supra*, n. 8, at p. 961, footnote 43.

> flexible wrapping materials meant only that the demand elasticity faced by du Pont was greater than one, this high cross-elasticity, far from proving a lack of market power, was a necessary condition of market power.[37]

Stegemann[38] highlights an additional variable which, if ignored, may lead to enormous policy options being deduced from the consideration of cross elasticities. The author postulates that, given an absolute change in the quantity demanded of a product, the value of the cross elasticity coefficient depends upon the initial size of the comparison good's market:

> The larger the market, the lower the coefficient [of cross elasticity] for margarine...If the size of the market influences the value of the coefficients for individual goods, it may also distort a comparison between them.[39]

As a consequence, if cross elasticities are used to determine market power a monopolist might well disguise his market power by setting the price of his product high and restricting his output.

Needham[40] also addresses the problem of using cross elasticities to estimate substitutability and, in addition to the difficulties mentioned above, consider two further conceptual problems. First, even if all goods could be ranked in order of fungibility, cross elasticity does not assist in ascertaining the threshold:

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[37] Ibid. See also: Supra, footnote 15.

[38] Klaus Stegemann, "Cross Elasticity and the Relevant Market," (1974) 94 Zeitschrift fur Wirtshaftsund Sozialwissenschaften 151.

[39] Ibid., at p. 154.

[40] Douglas Needham, "The Problem of Market and Industry Delineation," in The Economics of Industrial Structure, Conduct and Performance, Holt, Rinehart and Winston (1978) at p. 109.

> A crucial problem remains. Where does one draw the line between successive cross-elasticity magnitudes, thereby deciding which goods are to be regarded as the 'same' and which 'different', and therefore deciding also which firms are regarded as being members of the 'same' industry.[41]

Second, the coefficient of cross elasticity does not account for the existence of the feedback-response mechanism:

> Another point to bear in mind is that measures of substitutability, such as cross-elasticity of demand, refer to the extent to which one firm would lose or gain sales in response to a change in another firm's price, assuming that the first firm did nothing in response to the price change. This, and not the actual change in the quantity of the first firm's product demanded, which will depend upon the response of the firm to the price change, is the relevant measure if one is attempting to measure the degree of substitutability between products.
>
> Of course, this increases the problems associated with any attempt to obtain measures of cross-elasticity, because reactions by firms producing close substitutes for the product of a firm initiating a price change are often likely to occur in practice. However, it is important to distinguish clearly between the use of cross-elasticity measures as an indicator of substitutability, and as a indicator of the type of behavior resulting from close substitutability.[42]

Wenden recognizes that the monopolist is only concerned with his own price elasticity; the monopolist is not concerned with the changes in quantity demanded of other products as he increases his price. The magnitude of cross elasticity is not necessarily conclusive; it is relevant only because it is related to own price elasticity of demand.[43]

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[41] Ibid., at p. 113.
[42] Ibid., at p. 114.

(d) The Relevant Geographic Market

Once the relevant product market has been defined, only the subset of producers who can easily and inexpensively shift production to supply the product will be included in the market. This provisional geographic market does not, however, determine the total amount of foreign sales that will ultimately be included in the definition of the relevant market. For example, the initial response may be to include only the actual sales which are made in the merging firms' distributional area. Notwithstanding their propensities at the prevailing price, if the price is subsequently increased in the domestic market, foreign firms may be able to divert some of their sales from other areas into this market. Several commentators[44] have expounded on what has been described as the "Diversion Theory":

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[43] See: G. Werden, "Market Delineation and the Justice Department's Merger Guidelines," (1983) Duke Law Journal 514, at p. 573.

> We argue that if a distant seller has some sales in a local market, *all* its sales, wherever made, should be considered a part of that local market for purposes of computing the market share of a local seller. This is because the distant seller has proved its ability to sell in the market and could increase its sales there, should the local price rise, simply by diverting sales from other markets.[45]

Mathematically, the firm elasticity of demand, η_i^D , will be positively correlated to r_j , the ratio of the foreign firm's sales in all markets to that firm's sales in the local market, as follows:[46]

$$\eta_i^D = \frac{\eta_m^D}{S_i} + \frac{r_j \eta_j^S (1 - S_i)}{S_i} \quad . \qquad (6)$$

Intuitively, the rationale for this relationship stems from the idea that a fringe supplier selling a large proportion of his sales in other markets can more easily divert sales to the domestic market in response to a small price increase. As Landes and Posner state:

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[44] See: P. Areeda and D. Turner. *Antitrust Law* (1978), at p. 523(a); R. Posner. *Antitrust Law: An economic Perspective*. Chicago: University of Chicago Press (1976) at p. 133; Elzinga and Hogarty, "The Problem of Geographic Market Delineation in Antimerger Suits." *Antitrust Bulletin* 18 (1973) 45. Areeda and Turner argue that if a foreign producer makes some sales in the market, his total output should be included *unless* the product is regularly exported as well as imported *and* the sum of the foreign price plus transportation costs exceed the domestic price. Landes and Posner reject these caveats on the grounds that the products need not be perfect substitutes and minor product differentiation will be tolerated by monopolists who maximize long-run profits.

[45] *Supra*, n. 8, at p. 963.

[46] See *supra*, no. 8, Appendix at p. 987.

> The higher that ratio [r_i], the higher their supply response will be, because it is easier for distant sellers to divert a small fraction of their output to the local market should price rise there than it would be to divert a large fraction of their output to the local market.[47]

The policy implementation of the diversion hypothesis is to include all sales, wherever made, by a foreign firm with some sales in the provisional market, in the relevant market of the domestic seller:

> The simplest way to take account of the relationship between the distant sellers' sales in other markets and their supply response in the local market is to include those sales in the relevant market - in other words, to include in the local market the entire output of any seller who has some local sales.[48]

Landes and Posner make the novel argument that the local seller's market power can be measured independently of the foreign seller's transportation costs. If the foreign seller is presently selling some production in the domestic market and if he has a large inventory of sales which can be diverted from other areas, the domestic seller's price will be restrained by risk of new entry by the foreign seller. The domestic seller will resort to limit pricing.

> What is important is thus not any transportation cost or other barrier that foreign producers may face but (1) the fact that they sell some output in the local market and (2) the size of their total output, wherever sold, relative to the size of the local market in question. The fact that they sell some output in the local market indicates that any transportation cost or

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[47] Ibid., at. 963.
[48] Ibid., at p. 964.

> other distance-related barrier has been overcome so far as that output is concerned. The size of their total output relative to the size of the local market indicates the probable ease with which they can expand their output in the local market without incurring substantially higher costs of production. This relation is automatically captured by including their total output in the local market.[49]

Landes and Posner foresee a risk of strategic behaviour; the domestic firm may price to induce some foreign sales in his market in order to have all foreign sales included and dilute the relevant market.[50] However, the authors speculate that firms would be unwilling to risk allowing foreign competition a "toehold" in their market.

Furthermore, if the foreign firm does not sell any of its production in the market at present "but could do so if price were even slightly above marginal cost"[51] then the approach outlined above by Landes and Posner will still tend to oversate market power. "Their [foreign and fringe firms] ability [emphasis added] to sell in the market will not be registered in our market share computation.[52]

The reason for the foregoing reservation and caution is discovered by inspecting the concept of a firm's ability to compete in the domestic market. the authors extend the diversion theory by recommending that total capacity, rather than total sales, of foreign producers should be included in the market delineation because the unused, uncommitted, capacity operates as the effective constraint on market power. As Landes and Posner note:

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[49] Ibid.

[50] Ibid., at p. 965; see footnote 46.

[51] Ibid., at p. 967.

[52] Ibid., at p. 968. Note: This appears to be the academic genesis, or at least resurrection, of the "five percent test" employed ubiquitously in the 1984 Guidelines. See: section 2.11, for example.

> Unused capacity implies a high supply elasticity of the competitive fringe because such capacity can be brought into production promptly and with no increase in production costs; hence it is an effective constraint on the pricing of the local seller. (Of course, as noted earlier, it will not always be easy to determine what portion of a firm's unused capacity is really "excess" and so available to meet an increase in demand, as distinct from capacity that is needed as reserve capacity or that is obsolete and could be brought back into service only at high cost.)[53]

The final corollary to the diversion theory addressed by Landes and Posner suggests a procedure for dealing appropriately with product differentiation. If the product is imported because the consumer views the import as somewhat different than the domestic product, then prima facie that product should not be included in the market. However, the domestic monopolist could exclude the product by limit pricing, but may, instead, decide to give up a small percentage of his market share. The two authors propose two alternate solutions:

> There are two ways to deal with this problem. One is to require, in the case of a differentiated product, that imports cross some percentage threshold of the domestic market before the entire output of importing foreign producers may be included in that market. The

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[53] Ibid., at p. 966.

> idea is that it would probably not be optimal for a domestic monopolist to set a price that surrendered a large market share to foreign competitors. The second response would be allow the plaintiff to exclude foreign production upon a showing of very large transportation and/or tariff barriers not offset by lower costs of foreign production, implying that such imports as occur are due to consumer preference for a differentiated foreign product. Under either approach, even in the case of a differentiated product, foreign output would be presumptively includable in the domestic market upon a showing that foreign imports were occurring.[54]

With regard to true foreign competition in the international sense, as contrasted with fringe firm expansion, Landes and Posner recommend:

> To the extent available information permits, market shares will be assigned to foreign competitors in the same way in which they are assigned to domestic competitors.[55]

This concept of equity has been adopted unconditionally by the DOJ in the 1984 Guidelines:

> The analysis in this Section applies, as our choice of terms suggests, to the case where the distant seller is foreign as well as to the case where it is located in another part of the United States. With the growing importance of foreign trade in the U.S. economy, this point has fundamental importance for antitrust litigation.[56]

To this point, the discussion has focused on importation into the relevant market; one must also consider whether the sales which are exported by a firm in the domestic market should be included in the relevant product market.[57] Landes and Posner argue convincingly that the value of these exports should be included in the denominator of the market share because:

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[54] Ibid., at p. 965. Note: The 1984 Guidelines have accepted the second approach. See: Section 2.4, where the DOJ will use capacity figures where the products are not differentiated, sales figures where they are differentiated.

[55] Ibid., at p. 966.

[56] Supra, n. 1, Section 2.4, at 4492.40.

> Foreign production still constrains the domestic firm's market power because an increase in foreign production would reduce the domestic firm's exports, which would in turn induce it to divert supply to its domestic market, thereby reducing price in that market. The domestic firm's exports also enhance its power in the local market. By reducing exports it could raise the price of its product abroad, and this would make diversion by foreign producers to the U.S. market less attractive and so make it easier for the domestic firm to maintain a high price in that market.[58]

In the context of the DOJ's "five percent test," to be discussed below, it is important to realize the Cellophane problem cannot arise when calculating the geographic market. When determining the product market, an extemely high price of the investigated product may artificially create substitutes; it is improper to include these goods in the relevant market for the reason that they are substitutes solely due to the abnormally high price. On the other hand, when estimating the geographic market, it is already presumed that the goods are perfect substitutes. Consequently, a high domestic price can be restrained by foreign products whose foreign price plus transportation costs are lower. As expressed by Landes and Posner:

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[57] Supra, n. 8, footnote 51. See Marfels. "The Impact of Foreign Trade on Concentration Levels: Empirical Findings for Canadian Manufacturing Industries and for the Steel Industries of Four Countries," 24 Antitrust Bulletin. (1979) 12i; Sichel, "The Foreign Competition Omission in Census Concentration Ratios: An Empirical Evaluation." 20 Antitrust Bulletin (1975) 85, who argue that the sales exported from the domestic market should be ecluded from the market definition.

[58] Ibid., at p. 968.

> The key to this conclusion, however, is the assumption in our model that the distant sellers are sellers of the *identical* product. That is why only a cost disadvantage can keep them out of the market. . . .
>
> In the case of distant sellers of the same product, there is no distinction between the marginal and intramarginal purchaser; since the products are identical, each purchaser is as satisfied with the distant as with the local seller's good. While the seller of the substitute product may be competing only for the marginal purchase, the distant seller of the identical product is competing for *all* the local seller's customers.[59]

(e) The Effect of Mergers On Market Power

A generally accepted misconception exists that horizontal mergers increase the market share of the post-merger enterprise. This deduction is only valid if the following three assumptions are satisfied:

(a) No efficiencies or economies of scale are present or possible as a result of the merger,

(b) The elasticity of supply of the fringe element, n_j^S , is zero, and

(c) the merged firm does not collude with other members.

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[59] *Ibid.*, at p. 971.

If one recognizes that there does exist the possibility of entry, either by way of expansion or entry *de novo*, then the post-merger market share of the two firms combined will be less than their separate pre-merger market shares aggregated.

The effect of the merger is to incrementally *increase*, in most cases, the level of market power enjoyed by the merged firms. Assuming marginal costs and demand and supply elasticity do not change as a result of the merger, the incremental effect on market power, $\Delta L = P'-P/P$, reduces to:

$$\frac{P'-P}{P} = \frac{S'-S(\eta_m^D+(1-S')\eta_j^S)/(\eta_m^D+(1-S)\eta_j^S)}{\eta_m^D + (1-S)\,\eta_j^S - S'} \qquad (7)^{**}$$

where,
(a) the superscript (') denotes post-merger values,
(b) S is the market share of the larger of the two firms, and
(c) S' is the market share of the merged firm *after being adjusted to reflect the merger*.

It is essential to recognize that the post merger market share to be substituted into equation (7) has been

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[**] See: Appendix E for the derivation of equation (7).

previously adjusted to reflect the effects of the merger.

In the simple case where η_j^S is assumed to be zero, equation (7) reduces to:

$$\Delta L = \frac{P' - P}{P} = \frac{(S' - S)}{(\eta_m^D - S')} \quad . \qquad (8)$$

Consequently, the change in market power is always positive. If the constraint is relaxed to allow for positive fringe firm entry, the incremental change in market power will be less, but still positive.

If it is assumed that efficiencies do not result, but new entry does occur following a merger, the decrease in firm elasticity of demand will elevate prices. This rise in price will induce an increase in fringe firm production into the domestic market. As a result, the market share of the merged firm will be less than the combined market share of the pre-merger firms.

> Since the competitive fringe will expand output in response to the price increase and the merged firm will reduce output, the market share of the merged firm will be less than the combined market share of the two firms before the merger. Thus S cannot be computed simply by summing the premerger shares.[61]

Alternatively, if economies of scale and efficiencies dominate, marginal costs will fall, price will diminish and fringe firms will be induced to reduce their output. The merged firm must expand its output; hence its market share will rise. In sum, a merger will invariably increase market power; but its post-merger market share will rise if an increase in market power dominates and will fall if efficiencies prevail.[62] It is left for further study to determine the mechanism by which the post-merger share, S', can be estimated.

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[61] Supra, n. 8, at p. 972.

Although Landes and Posner do not address the issue directly, it is submitted that if, in the first analysis, the delineation of the market accounted for substitutability in production of the fringe firms, the post-merger market share would not have to be adjusted "to reflect the merger."[63] Simply stated, the supply elasticity would be incorporated at the market delineation stage; accordingly, the outcome of a merger would always precipitate an increase in market share.

The application of the HHI in the 1984 Guidelines to monitor the effects of a merger on market power relies crucially on this deduction. As the 1984 Guidelines indicate:

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[62] Ibid., at p. 973; "There is a simple test, in principle, for comparing an increase in efficiency with an increase in market power. When economies of scale dominate, the market shares of the firm resulting from the merger will be greater than the sum of the shares of the acquiring and acquired firms. When an increase in market power dominates, the resulting firm's share will be smaller. Of course, this test cannot be used in a proceeding to enjoin a merger before it takes place; and its use even in cases involving consummated mergers is of doubtful utility since the merged firm may deliberately keep price low during the pendency of the merger case in order to pass the test."

[63] Ibid., at p. 972.

> 3.0 Where the merging firms are in the same product and geographic market, the merger is horizontal. In such cases the Department will focus first on the post-merger concentration of the market and the increase in concentration caused by the merger.[64]

The change in the HHI due to the merger measures the increase in concentration in the relevant market and utimately the incremental change in market power.[65] This increase in the HHI presupposes an increase in market shares; in turn, the market share increases rely upon the proper inclusion of fringe elasticity of supply in the *a priori* market delineation.

In addition to market elasticity of demand[66] and the level of marginal costs,[67]

> "a more important limitation of the use of equation (4) [equation (7) above] is that it assumes (as we have generally done in this Article) that the firm resulting from the merger does not collude with the other firms in the market; that any market power it exercises is strictly unilateral."[68]

In short, the "collusion theory" of oligopolistic behaviour has been ignored. Alternately, the market power which is realized as a result of a merger is contingent on the establishment of monopoly power alone. Landes and Posner are not unmindful of this pretermission:

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[64] *Supra*, n. 1, at 4493, section 3.0.

[65] The conceptual problems with the HHI - concentration - market power causal link are discussed in the chapter on measuring competition, *supra*.

[66] Fringe firm elasticity of supply is subsumed under demand elasticity in this context.

[67] Efficiencies, economies of scale and X- inefficiencies all may affect marginal costs.

[68] *Supra*, n. 8, at p. 973.

> But a horizontal merger is more likely to facilitate collusion by reducing the number of firms that must agree for collusion to be effective, and thus the transaction costs of agreement, than it is to create a dominant firm or to enhance the power of such a firm; and this effect is not captured in our formal apparatus.[69]

This preceding theoretical foundation for the U.S. Merger Guidelines spotlights the major weakness in the mechanical application of the HHI; the 1984 Guidelines attempt to remedy this shortcoming by injecting into the analysis other qualitative factors which should be considered in light of the "collusion theory".[70] For injunctive guidelines in the Canadian setting, these qualitative factors may play a subordinate role.

In an attempt to summarize the essential concepts of the foregoing discussion, one must recall that three principal variables can affect the degree of market power:

(a) Firm elasticity of demand (monopoly power),

(b) Marginal costs (efficiencies), and

(c) Collusion.

The investigation into the market power repercussions of merger activity should converge on the various factors which influence these three target variables. With regard to provisional relief, emphasis should be placed on the first variable, due to the availability of a practical monitoring procedure and the preliminary nature of the relief sought. The latter two variables are considered more appropriate to an adjudication on the merits. If merger proscription is to be aimed primarily at large mergers in dominant sectors, guidelines which trigger administrative interest in provisional relief may rely on a prima facie test of concentration, recognizing that the market elasticity of demand factors must be incorporated in the determination of the relevant market. As Landes and Posner conclude:

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[69] Ibid.

[70] Supra, n. 1, see: sections 3.2 to 3.5.

> Our analysis may still be useful in the horizontal merger context. First, some horizontal mergers may be so large that they create market power in the sense captured by our analysis: the power to raise price without collaborating with (or intimidating) other firms. Indeed, when a firm is accused of monopolizing and the only significant monopolizing practice alleged is mergers (as in the old U.S. Steel monopolization case), our analysis, or something akin to it, is a necessary foundation for a finding of violation.[71]

2. THE RELEVANT MARKET DELINEATION IN THE 1984 GUIDELINES

(a) Market Definition

From the foregoing analysis, it has become apparent that the determination of the degree of market power arising from a merger is predetermined by the delineation of the market in which firms might exercise control over price. The Guidelines define a market as,

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[71] Ibid., at p. 974.

> [A] product or group of products and a geographic area in which it is sold such that a hypothetical, profit-maximizing firm, not subject to price regulation, that was the only present and future seller of those products in that area would impose a "small but significant and nontransitory" increase in price above prevailing or likely future levels. The group of products and geographic area that comprise a market will be referred to respectively as the "product market" and the "geographic market."[72]

The market is artificially segmented into the "product market" and the "geographic market". The probable demand reponses of consumers and the potential supply responses of producers are conjunctively exploited to adjust the original provisional market:

> A price increase could be made unprofitable by any of four types of demand or supply responses: (1) Consumers switching to other products; (2) consumers switching to the same product produced by firms in other areas; (3) producers of other products switching existing facilities to the production of the product; or (4) producers entering into the production of the product by substantially modifying existing facilities or by constructing new facilities. Each type of response is considered under the Guidelines.[73]

The Guidelines emphasize that historical market information will be the basis for predicting probable future reponses.

The history of the American jurisprudence sets the stage for the theoretical notions subsequently adopted in the 1984 Guidelines. As early as 1953, the U.S. Supreme

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[72] Supra, n. 1, section 2.0.

[73] Ibid.; See: Appendix G for a comprehensive flowchart of the 1984 Guidelines.

Court, in the *Times-Picayune* case, realized that the market boundaries were sensitive to the degree of price variation. If the price is high enough, any product has a substitute:

> For every product, substitutes exist. But a relevant market cannot meaningfully encompass that infinite range. The circle must be drawn narrowly to exclude any other product to which, *within reasonable variations in price* [emphasis added], only a limited number of buyers will turn; in technical terms, products whose 'cross-elasticities of demand' are small. Useful to that determination is, among other things, the trade's own characterization of the products involved. The advertising industry and its customers, ~~for example~~, markedly differentiate between advertising in newspapers and in other mass media.'[78]

Again in 1956, the Supreme Court perceived that, conceivably, all products may be substitutes:

> For example, one can think of building materials as in commodity competition but one could hardly say that brick competed with steel or wood or cement or stone in the meaning of Sherman Act litigation; the products are too different. This is the interindustry competition emphasized by some economists.'[79]

The court continued in the *Cellophane* case to establish what is presently referred to as the "reasonable interchangeability test.":

> Every manufacturer is the sole producers of the particular commodity it makes but its control...of the relevant market depends upon the availability of alternative commodities for buyers: i.e., whether there is a cross-elasticity of demand between cellophane and the other wrappings. This interchangeability is largely gauged by the purchase of competing products for similar uses considering the price, characteristics and adaptability of the competing commodities.

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[78] *Times-Picayune* v. *U.S.*, 345 U.S. 594 (1953), at p. 612, n. 31.

[79] *U.S.* v. *E.I. du Pont de Nemours & Co.* (Cellophane), 351 U.S. 377 (1956), at p. 393.

> . . . .
>
> Determination of the competitive market for commodities depends on how different from one another are the offered commodities in character or use, how far buyers will go to substitute one commodity for another.
>
> The varying circumstances of each case determine the result. In considering what is the relevant market for determining the control of price and competition, no more definite rule can be declared than that [it consists of] commodities reasonably interchangeable by consumers for the same purposes...[74]

Broad markets were circumscribed by the frequently referenced doctrine of "sub-markets" expounded by the Supreme Court in the Brown Shoe judgment. Practical indicia were sought to define the relevant market; however, the court in Brown Shoe was also reiterating the Cellophane test:

> The outer boundaries of a product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself

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[74] Ibid., at pp. 380, 393, 395.

and substitutes for it.[77]

In Brown Shoe, examples of "practical indicia" of cross-elasticity of supply are cited as commonality of product, technological adaptability, separate facilities, supplier specialization and diversification trends.

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[77] Brown Shoe Co., Inc. v. U.S., 370 U.S. 294 (1962), at p. 325. See also: U.S. v. Philadelphi National Banks, 374 U.S. 321 (1963), 356, for the "cluster of products" concept with respect to the product market. The Court acknowledged the necessity of establishing the geographic boundaries, but opted for an intuitive compromise seemingly short on economic justification. As the Supreme Court explained:

> ...that...the relevant geographical market is a function of each separate customer's economic scale means simply that a workable compromise must be found: some fair intermediate delineation which avoids the indefensible extremes of drawing the market either so extensively as to make the effect of the merger upon competition seem insignificant, because only the very largest bank customers are taken into account in defining the market, or so narrowly as to place appelees in different markets, because only the smallest customers are considered. We think that the four-county Philadelphia metropolitan area...which would seem roughly to delineate the area in which bank customers that are neither very large nor very small find it practical to do their banking business, is a more appropriate "section of the country" in which to appraise the instant merger than any larger or smaller or different area.

See: Philadelphia National Bank, at p. 361. See also: U.S. v. Von's Grocery Co. et al., 384 U.S. 270 (1966), for a general acceptance of the submarket concept, in this case retail grocery sales in the greater metropolitan Los Angeles area.

In the *Continental Can* case, the court turned to what has been labeled the "end use doctrine" to determine substitutability.[78] Continental, which was the nation's second largest manufacturer of metal containers with a market share of thirty-three percent, acquired Hazel-Atlas, the third largest producer of glass containers with a market share of approximately ten percent. The Court contended that the interindustry competition between the two was sufficiently great to warrant defining a combined metal and glass container market as a separate line of commerce. In 1966, the U.S. Supreme Court came very close in the *Grinnell* case to establishing the forerunner of the present "five percent test." The Supreme Court stated its position on substitutability as:

> a product...may be of such a character that substitute products must also be considered, as customers may turn to them if there is a slight increase in the price of the main product.[79]

In *Alcoa-Rome* another approach to the concept of market definition focused on the sale of different products, for the same use, to the same customer.[80] Alcoa, the leader in production of aluminum conductor wire with a market share of twenty-eight percent, merged with the Rome Cable Co., a producer of copper wire accounting for 1.3 percent of the market. Although the district court held that aluminum and copper wire fall within the same market, the Supreme Court found that aluminum conductor wire was a "submarket". The preceding enumeratopm of judicial attempts to define the relevant market is not complete;[81] however, one cannot escape the inevitable conclusion that with the exception of the obiter in Brown Shoe, the courts were preoccupied with demand substitutability, at the expense of supply and geographic substitutability.

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[78] *U.S.* v. *Continental Can Co.*, 378 U.S. 441 (1964); affirming District Court 217 F.Supp.794, at p. 796.

[79] *U.S.* v. *Grinnell Corp.*, 384 U.S. 563 (1966), at p. 571.

[80] See: *U.S.* v. *Aluminum Co. of American*, 377 U.S. 271 (1964), 275. Note that the similarity of buyers, however, is not an indicia of supply substitutability. See: *U.S.* v. *Citizens Publishing Co.*, 394 U.S. 131 (1969); *U.S.* v. *El Paso Natural Gas Co.*, 376 U.S. 651 (1964).

Brock[82] categorizes three major thrusts by economists to define the "relevant market": First, attempts have been initiated, with mixed success, to determine more theoretically acceptable methods of delineating both product and geographic boundaries.[83] Second, market thresholds have been proposed which would trigger merger proscription.[84] And finally, attempts have been made to increase the meaningfulness and usefulness of market share data.[85] On reviewing these theories, Brock concludes with a suggested "shopping list" of factors which may affect the determination of the relevant market; practically all of these parameters have been included, at least implicitly, in the 1984 Guidelines.

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[81] For a detailed overview of the American jurisprudcence, see: G.S. Rosenthal, "Continental Can Revisited: Limits on the Breadth of a Line of Commerce in a Section 7 Case," (1977) 14 Houston Law Review 973. See also: J.E. Fortenberry, "Definition of Markets in Merger Cases: Developments Since The 1968 Department of Justice Merger Guidelines." (1982) 25 Howard Law Journal 595 for a good review of the American judicial pronouncements on relevant markets.

[82] J.W. Brock, "Industry Structure," (1984) 29 Antitrust Bulletin 535.

Werden[86] in a comprehensive and well reasoned article, emphasizes the neglect, in both the literature and the jurisprudence, of incorporating supply substitution into the definition of the relevant market. Werden suggests that three conceptual methods are available to adjust market boundaries for supply elastcity:

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[83] See: I. Horowitz, "Market Definition in Antitrust Analysis: A Regression-Based Approach," (1981) 48 Southern Economic Journal 1; See also: (1982) 49 Southern Economic Journal 559, (1982) 49 Southern Economic Journal 564; K. Boyer, "Industry Boundaries," Economic Analysis and Antitrust Law, edited by Calvani and Siegfried (1979); K.G. Elzinga, "Defining Geographic Market Boundaries," (1981) 26 Antitrust Bulletin 739; G.J. Werden, "The Use and Misuse of Shipments Data in Defining Geographic Markets," (1981) 26 Antitrust Bulletin 719.

[84] See: A. White, "The Dominant Firm Structure: Theoretical Myth or Empirical Reality?" (1981) 48 Southern Economic Journal 427; J. Kwoka, "The Effect of Market Share Distribution in Industry Performance," (1979) 61 Review of Economics and Statistics 101.

[85] See: Landes and Posner, supra, n. 8, for a review of the literature.

[86] G.J. Werden, "Market Delineation and the Justice Department's Merger Guidelines," (1983) Duke Law Journal 514.

(1) MARKET DELINEATION APPROACH

Initially, all products that are capable of being produced by the merging firm are defined as the relevant product. To determine the relevant product market, all firms that are capable of producing the foregoing relevant product are included.

(2) SHARE MEASUREMENT APPROACH

Initially, determine all the firms that are capable of producing the same product as the merging firm's product. All these firms' products will define the relevant product. Then determine all the firms that produce the relevant product in order to circumscribe the relevant product market.

(3) SHARE SIGNIFICANCE APPROACH

The market is defined to include only the product of the merging firm, but the resultant market share is discounted for supply substitution.

Obviously, without constraints, the three approaches should yield identical results. However, approach (2) appears to have been adopted by the DOJ for several reasons. An explicit incorporation of supply substitution at the market delineation stage will avoid its possible oversight. Additionally, market constraints which are usually present, are more easily accounted for when measuring market shares. And finally, one might wish to distinguish between supply substitution and barriers to entry; if this is the case, analysis of ease of entry might be relegated to post share-calculation adjustment.

(b) Determination of the Relevant Product

The initial step is to determine the "provisional relevant product"; all products which are identical to those produced by the merging firm are to be included in this categorization. The second stage is to evaluate whether the product is perceived by the customers of the merging firm as a good substitute at prevailing or likely future prices.[87] This demand substitutability optimally is determined at likely future prices because the effect of the merger is monitored for a non-transitory period of one year. Due to the fact that such price data may not be available:

> In the above analysis, the Department will use prevailing prices of the products of the merging firms and possible substitutes for such products. However, the Department may use likely future prices when changes in the prevailing prices can be predicted with reasonable reliability. Changes ~~in~~ price may be predicted on the basis of, for example, expected changes in costs or demand caused by changes in environmental regulations or expected changes in regulations that directly affect price.[88]

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[87] *Ibid.*, at p. 526 for discussion of "prevailing" versus "competitive" prices and "prevailing" versus "likely future" prices.

[88] 1984 Guidlines, *supra*, n. 1, section 2.11. Note: This is a positive change from the 1982 Guidelines, 4502.10, n. 9.

The third step proposes what has come tc be known as the "five percent test." The Guidelines embrace the concept of firm elasticity of demand, which had been so vigorously exhorted by Landes and Posner, by proposing to observe whether consumers would shift to the product due to a "small but significant and nontransitory"[89] increase in the price.[90] As a first approximation, the DOJ will query whether a hypothetical single seller of the group could profitably[91] maintain a hypothetical five-percent increase above the prevailing or likely future price levels for one year.[92]

Several caveats must be applied to the five percent test. First, as the price is increased, only the "next best substitute" will be added to the provisional product. This averts the discontinuity problem which could arise by expanding the market for cellophane wrapping by adding matches to the group and applying the five percent test.[93] Second, the DOJ will apply the "smallest market" rule:

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[89] *Ibid.*, 4492.101; See: Werden, *supra*, n. 86, at p. 545 *et seq.* where the author expounds on the problems associated with setting this price threshold.

[90] The "price" is the price of the provisional product. See: 4492.101, note 6.

[91] See: Werden, *supra*, n. 86 for a discussion of the problems in defining the term "profitable". Werden suggests that three possible interpretations exist: (1) an increase in economic profits from the *status quo*, (2) a preclusion in any decrease in the present level of profits, and (3) a guarantee of some minimum level of profits.

[92] *Supra*, n. 18; Buyers and sellers are assumed to immediately recognize the price increase and believe that it will be maintained in the future. See also: footnote 10 (1982 Guidelines). Note: Werden argues that ten percent is a more appropriate level.

> The Department generally will consider the relevant product market to be the smallest group of products that satisfies this test.[94]

The practical application of the demand elasticity test may be based on circumstantial evidence.[95] The first discussion of the five percent test in the literature[96] reviews the methodology and limitations arising from its use in *U.S.* v. *Virginia National Bankshares Inc*.[97] The crucial issue in the case centered on whether two provisional geographic markets for local banks were to be treated as one unified relevant geographic market or whether they were to be segmented. A questionnaire, which was designed by the DOJ to apply the five percent test to banking, enquired whether the bank customer would go outside his home community in order to save five percent on loan interest charges. The answers to the questionnaire, along with expert testimony, were tendered in evidence at trial. Approximately forty-two percent of all responding commercial loan customers replied that they would transfer to a bank at least one town away if they could save five percent on a loan. On the basis of this evidence, the DOJ contended:

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[93] See: Werden, *supra*, n. 86, at p. 528.

[94] *Supra*, n. 18; Werden, *supra*, n. 86, at p. 540, proposes a "minimax" solution.

[95] See: Footnote 10 (1982 Guidelines). This footnote is omitted in the 1984 Guidelines. However, no inference is to be drawn of a policy change from the omission of a footnote (4490).

[96] R.J. Wertheimer, "DOJ Tries Out Its 5-Percent Geographic Market Test," August (1982) *Legal Times*, 17-18; See also: D.L. Flexner, "Client Counseling and the Merger Guidelines: New Opportunities for Advocacy," *New Merger Guidelines*, ed. Schenefield, Practising Law Institute, (1982), for practical hints on approaching the "five percent test."

[97] *U.S.* v. *Virginia National Bankshares Inc.*, 1982-2 CCH Tr. Cas. 64,871 (W.D. Va. 1982).

> [T]hat substantial numbers of bank customers were prepared to divert their business from banks in their home communities to banks elsewhere in Wise County - but not outside Wise Country - in response to a 5 percent price differential. Therefore, the division contended, the survey showed that all the banks in Wise County - and certainly all the banks in Wise/Norton and Coeburn - should be considered competitors of one another in a single geographic market. In the words of the merger guidelines, the division contended that even though Wise/Norton and Coeburn were not in the same provisional market, the 5-percent test shows that they ultimately belong in the same banking market.[98]

The defendants challenged this hypothetical method of defining the relevant geographic market on three primary grounds. First, the defendants submitted that the proper test to define the geographic market in a banking case was not the "five percent test" promoted by the DOJ Guidelines but the test set forth by the Supreme Court in the Philipsburg National Bank[99] and Southwest Mississippi Bank[100] cases. These cases established a three part test: where do the merging banks have their offices, where do they draw their business and where do they solicit business. Second, testimony of local bankers from both sides indicated that banking was extremely localized and that banks could not compete in an area without establishing a branch. Finally, the defendants also challenged the reliability of the survey evidence, on the following grounds:

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[98] Supra, n. 96, at p. 17.
[99] U.S. v. Phillipsburg National Bank and Trust, 399 U.S. 35D, 362 (1970).
[100] Southwest Mississippi Bank v. FDIC, 499 F. Supp. 1, 11, aff'd 625 F.2d B1013 (5th Cir. 1980).

(a) Survey responses were very low,
(b) 1The survey employed leading questions, and,
(c) The five percent question was unrealistic in many respects.

In future cases the first two difficulties may be avoided by utilizing experts in survey analysis, possibly from the Department of Consumer and Corporate Affairs.[101] The third limitation embodies three troublesome conceptual problems. First, the survey asked respondents to assume a five percent price differential that had not been solicited; the test assumed that transaction costs were zero.

> [T]he 5-percent question unrealistically asked the respondent to assume that the 5-percent saving somehow plopped into his lap unsolicited, without any effort or initiative on his part. It did not ask whether the respondent would shop for a lower interest rate by driving to or calling banks outside his home community, but asked the respondent only if he would have taken a cheaper loan if a cheaper loan had been offered to him. Unsolicited offers of cheaper loans are uncommon.[102]

Second, the geographic market test must determine whether new suppliers will enter the provisional market due to a

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[101] To preserve the appearance of impartiality, it is recommended that the survey be commissioned to an independent, non-governmental agency.

[102] Supra, n. 96, at p. 18.

"small but significant and nontransitory" price increase, not whether the consumer will shift suppliers. Third, the survey queried customers to speculate on a price differential that had never existed and was not likely to exist in the future.

> The 5-percent test is in a sense a potential competition test: it presumes that potential sellers in the provisional market - sellers who are now outside the market but prepared to enter it in response to a 5 percent differential - impose a constraint upon the sellers now in that market. A court may doubt the practical constraining effect of potential competition premised upon a price differential that has not existed in the past, that does not exist at present, and that is highly unlikely to exist in the future.[103]

These shortcomings do not depregate the usefulness and efficacy of the "five percent test." The empirical survey must simply ensure that questions relevant to transaction costs are addressed. Additionally, the geographic market must be delineated with respect to producer, not consumer, shifts. And finally, the "five percent test" is more aptly suited to cases where there is historical evidence that buyers have actually switched business to sellers outside the provisional market in response to price changes. As Wertheimer concludes:

> [T]he 5-percent test may be more useful to the division and to private antitrust practitioners in analyzing mergers to determine whether a [Section] 7 case should be filed than in litigating a [Section] 7 case. In Virginia National, the division invoked the 5-percent test. However, I expect that more often than not,

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[103] Ibid., at p. 18.

> counsel for the merging parties will be the ones invoking the 5-percent test to enlarge the market and thereby reduce the market shares of the merging parties. In precomplaint merger analysis, courtroom rules of evidence and burdens of proof need not be observed. A survey insufficient to persuade a court to enjoin a merger may be sufficient to convince division economists that the provisional market should indeed be expanded, and no [Section] 7 complaint filed.[104]

The proposals for the Canadian setting adopt this proviso; the guidelines are to be restricted for use at the prelitigation stage for the purpose of directing the Bureau of Competition Policy and informing the business community.

The "five percent test" establishes only the first approximation of the relevant product. Other reliable circumstantial evidence may be considered to infer the likely effects of a future price increase. The 1984 Guidelines propose that these "other variables' include[105]:

(1) Evidence that buyers have actually shifted purchases between the products,

(2) Similarities in physical and technical characteristics,

(3) Similarities in long-run price movements, and

(4) Evidence that the sellers perceive the products as fungible, particularly with

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[104] Ibid., at p. 18.
[105] Supra, n. 1, at 4492.102, section 2.12.

> regard to business decisions.[106]

If these queries may be asnwered in the affirmative, then the relevant product will be expanded to include the appropriate close substitutes in demand.

Finally, the DOJ will consider restricting the relevant product to those products over which the merging firm may have the power to price discriminate.

> Even though a general increase in price might cause such significant substitution that it would not be profitable, sellers who can price discriminate could raise price only to groups of buyers who cannot easily substitute away. If such price discrimination is possible, the Department will consider defining additional, narrower relevant product markets consisting of particular uses of the product for which a hypothetical monopolist could profitably impose a "small but significant and nontransitory" increase in price.[107]

In the absence of price discrimination, the relevant product definition is retained. The second major step which follows is to identify the firms that produce the relevant product characterized in section 2.1.

(c) Relevant Product Market and Supply Substitution

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[106] Note: It does not appear pertinent that seller's perceptions should determine the relevant product. This variable might be included more appropriately in the determination of the relevant product market (section 2.21), where supply substitution is adjusted. See: Peter Bronsteen, "A Review of the Revised Merger Guidelines," (1984) 29 Antitrust Bulletion 613, at p. 641.

[107] Supra, n. 1, at 4492.103, section 2.13.

Once the products which comprise the relevant product have been determined, the magnitude of the market, in other words the denominator in the market share ratio, must be estimated. The 1984 Guidelines arrive at the determination of the relevant market by first establishing the bounds of the relevant product market, then possibly contracting this outer boundary by superimposing the requirement of geographic substitutionality. Ultimately, the relevant market will consist of the output and sales, or capacity, of all firms that would conceivably restrain the merging firm's potential market power.

The initial stage of defining the "relevant product market" contemplates whether the firm being considered for inclusion produces and sells the relevant product. If the response is in the affirmative, then the *total* production and sales of that specific firm is included in the relevant product market.[108] If the firm does not presently produce and sell any of the relevant product, its production may be included in the market if its production and sales facilities could easily and economically be shifted to the relevant product due to a "small but significant and nontransitory" price increase.[109] Again, as a first approximation, the DOJ will conjecture whether the firm is likely to shift production and sales to the relevant product within one year[110] due to a five percent price increase. If supply substitution is likely, the sales likely to be made or the capacity likely to be used due to an appropriate price increase would be included in the market.[111]

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[108] See: Landes and Posner, *supra*, n. 8, at p. 963, for an explanation of the inclusion of total sales, independent of transportation costs.

Supply substitution is defined by Karsch as:

> Supply substitution occurs when a firm engaged in the production of one good can shift its operations quickly and inexpensively to producing another good.[112]

The rationale for including the capacity of potential competitors in the relevant market is engendored in the principle of deterrence:

> The prospect of new firms entering a market in response to anticompetitive conduct by an existing producer deters the existing producer from raising price.[113]

Karsch postulates that the two fundamental parameters which affect the degree of supply substitution are costs and time:

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[109] *Supra*, n. 1, at 4492.21, section S2.21. See also: J. D. Pace, "The Changing Role of Supply Substitutability in Defining and Measuring Relevant Markets", *New Merger Guidelines*, ed. J. H. Shenefield, Practising Law Institute, (1982) at p. 103. for a general discussion.

[110] 1982 Guidelines, *supra*, n. 1, at 4502.201, section II B(1): The time period was set at six months.

[111] 1984 Guidelines, *supra*, n. 1, at 4492.40, section 2.4; The calculation of market shares again employs the one year "five percent test".

[112] B. Karsch, "The Role of Supply Substitutability in Defining the Relevant Product Market," (1974) 65 *Virginia Law Review* 129, at p. 131. See generally: P. Areeda and D. Turner *Antitrust Law* (1976) at p. 126; C. Kaysen and D. Turner *Antitrust Policy* (1959), at p. 27.

[113] *Ibid.*, at p. 131.

> When transition can be swift and inexpensive, however, the possibility of entry can constrain the exercise of monopoly power just as effectively as the presence of demand substitutes.[114]

The 1984 Merger Guidelines manifest complete acceptance of the concept of supply substitution; the relevant product market is determined by including those firms which would supply the relevant product if conditions changed. Similarly, a merger between an incumbent and a potential competitor may well eliminate the deterrent effect that competition might have on the realization of market power.[115]

Apart from present or potential future production and sales,[116] if the firm produces recycled or reconditioned goods that would be included in the relevant product, then the entire sales of that firm also should be included in the relevant product market.[117] Finally, the 1984 Guidelines envisage internal or captive consumption in vertically integrated industries frustrating overall market power. As the 1984 Guidelines state:

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[114] Ibid., at p. 133.

[115] For the leading cases in the area of supply substitution and potential competition in the United States, see: United States v. Connecticut National Bank, 418 U.S. 656 (1974); United States v. Marine Bancorp., 418 U.S. 602 (1974); United States v. Falstaff Brewing Corp., 410 U.S. 526 (1973); FTC v. Proctor & Gamble Co., 386 U.S. 568 (1967); United States v. Penn-Olin Chem. Co., 378 U.S. 158 (1964).

> Such [vertically integrated] firms may respond to an increase in the price of the relevant product in either of two ways. They may begin selling the relevant product, or alternatively, they may continue to consume all of their production but increase their production of both the relevant product and products in which the relevant product is embodied. Either kind of supply response could frustrate collusion by firms currently selling the relevant product. ~~If a~~ firm would be likely to respond either way to a "small but significant and nontransitory" increase in price will be determined in the same way in which it is determined in product

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[116] The concept of potential competition plays a dominant role in American antitrust policy; the principle is strikingly absent in the context of Canadian competition policy. The American courts have extended the concept to the point of distinguishing between actual potential competition (potential entry which will occur, whether the incumbent is aware or not) and perceived potential competition (potential entry which is expected to occur by the incumbent, notwithstanding the fact that it may never materialize). See: R.L. Hubbard, "Potential Production: A Supply Side Approach for Relevant Product Market Definitions," (1980) 48 Fordharm Law Review 1199. Supply substitution, elasticity of supply, production substitutability and potential competition are all, in essence, synonyms. Barriers to entry are frequently cited as the cause of decreased supply substitution. See also: Bruce Karsch, "The Role of Supply - substitution in Defining the Relevant Market," (1979) 65 Virginia Law Review 129. See also: United States v. Falstaff Brewing Corp., 410 U.S. 526 (1973), at p. 554.

[117] 1984 Guidelines, Supra, n. 1, at 4492.202, section 2.22, Durable Goods.

market definition.[118]

Note that in the case of internal consumption, in contrast to durable goods, only the relevant sales level or capacity is included in the market.[119]

Subsequent to the determination of the provisional relevant product market, an accounting for potential supply substitutability and other factors, adjustments must be made to the market if the products are differentiated. If the products are not identical, then capacity figures are to be used; if the products are differentiated, then actual sales figures more closely measure the dampening effect on the merging firm's potential for market power.[120]

In determining market shares, if the firm presently produces the relevant product, whether or not it has been recycled or reconditioned, then total production is included; if the firm can potentially shift production, whether or not the production is external or internal, then only the relevant sales determined by the "five percent test" will be included in the relevant product market.[121]

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[118] Ibid., at 4492.203, section 2.23, Internal Consumption.

[119] Supra, n. 111.

[120] 1984 Guidelines, Supra, n. 1, at 4492.303, section 2.4. See: Landes and Posner, supra, n. 8, at p. 965, for the rationale.

[121] Ibid.

(d) Foreign Competition

The final aspect of delineating the relevant product market, and an topic of utmost importance to the Canadian experience, confronts the competitive impact of foreign competition. The general intent of the 1984 Guidelines is to treat foreign competition in fashion no different than domestic competition.

> To the extent available information permits, market shares will be assigned to foreign competitors in the same way in which they are assigned to domestic competitors.[122]

The importance of including foreign competition in the relevant market should not be underestimated. As Abbott emphasizes:

> A decision to exclude foreign competition and define the relevant market on a national basis runs the risk that concentration ratios may overstate monopoly power. On the other hand, the inclusion of foreign competition in the market may understate potential monopoly power, to the extent that foreign firms would not be able to expand their supply (because of import restraints or for other reasons) in the event of a sustained price rise by domestic firms. In short, the treatment of foreign competition in the market definition process is of major policy significance.[123]

Landes and Posner,[124] encouraged by several earlier investigations,[125] argued:

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[122] Ibid., at 4492.40, section 2.4.

[123] Alden Abbott, "Foreign Competition and Relevant Market Definition under the Department of Justice's Merger Guidelines," (1985) 30 Antitrust Bulletin 299, at p. 299.

[124] Landes and Posner, "Market Power in Antitrust Cases," (1981) 94 Harvard Law Review (1981) 937, 964.

> Landes and Posner examined the factors that affect the extent to which a single dominant seller would raise price above marginal cost. They stressed that there is no real need to delineate markets to examine those factors where the elasticity of demand faced by the dominant firm readily can be measured. Where demand elasticity cannot easily be measured, they concluded that reliance on a relevant market definition would be called for. They then argued that, if there are significant imports of a product into the United States, the imports must be included in the relevant market and, moreover, that foreign producers responsible for imports should be assigned market shares based on their total production or capacity, regardless of the extent of their current exports to the U.S. They maintained that once a distant seller has proved its ability to sell in the market (by exporting to the market), it could increase its sales there in the face of a local price rise, simply by diverting sales from other markets.[126]

However, this assertion sparked much heated debate. Brennan[127] maintains that where the capacity to ship into the domestic market is fixed,[128] the local producer is not restrained from increasing his price by the foreign competition. As Abbott summarizes:

> More generally, Brennan demonstrated that Landes and Posner incorrectly defined the supply elasticity of imports.
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> . . . .

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[125] P. Areeda and D. Turner. Antitrust Law (1978) at par. 523a; R. Posner, Antitrust Law (1976), at p. 133; Elzinga and Hogarty, "The Problem of Geographic Market Delineation in Antimerger Suits," 18 Antitrust Bulletin (1973) 45.

[126] Supra, n. 123, at p. 302.

[127] Brennan, "Mistaken Elasticities and Misleading Rules," (1982) 95 Harvard Law Review 1849.

[128] For example, the modes of transport are operating at full capacity or are fixed in capacity, e.g., oil pipelines.

> The import elasticity is what Landes and Posner compute it to be only if this "price elasticity" equals one. If it is greater than one, the import elasticity is greater and domestic firms have less market power than Landes and Posner's measure would indicate. If it is less than one, their measure may understate the market power possessed by domestic firms.[129]

Kaplow,[130] in a response to Landes and Posner's extensive article, contends that foreign competition should not automatically be included in the relevant market merely because a degree of import penetration exists. The author argues that Landes and Posner's inclusion of foreign competition holds only if foreign and domestic products are perfectly identical. If the products are differentiated, then an increase in domestic prices may not induce a significant increase in importation.[131] Kaplow also asserts that foreign producers may face transaction costs switching to export production.[132] Schmalensee echoes this concern in cases where the market definition requires inclusion of products that are significantly differentiated:

> [O]ne can say nothing about the relation between a firm's demand elasticity and that firm's share of the market.[133]

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[129] Supra, n. 123, at p. 310.

[130] Kaplow, "The Accuracy of Traditional Market Power Analysis and a Direct Adjustment Approach," (1982) 95 Harvard Law Review 1817.

[131] Ibid., at p. 1836.

[132] Ibid., at p. 1843.

[133] R. Schmalensee, "Another Look at Market Power," (1982) 95 Harvard Law Review 1789, at p. 1800.

Ordover and Willig[134] strike a middle ground, accepting the significance of foreign production on market power but including only actual imports. In summation, another interested observer spotlights two fundamental problems with the treatment afforded foreign competition by Landes and Posner:

> First, the Landes and Posner argument assumes that the capacity in question is cost effective--that is, that it can be brought into production at a marginal cost within the relevant range. The dominant firm's ability to exploit market power clearly is limited if there exists a substantial amount of cost effective capacity overhanging the market. But obsolete, high-cost capacity is irrelevant. Second, the Landes and Posner analysis assumes that all producers supply identical products--there is no product differentiation and consumers have absolutely no preference of one supplier's goods over another's. From these two assumptions, it follows that if the price is right, there is no impediment to any supplier selling as much as he can possibly produce. Under these limited circumstances, it clearly is appropriate to view all rival capacity as placing an immediate constraint on the dominant firm's market power. Once you introduce product differentiation and upward sloping supply curves (i.e., additional output will be forthcoming only a successfully higher unit costs), the Landes and Posner argument, as they recognize, no longer follows.[135]

Abbott endeavors to synthesize the work of Landes and Posner with the concerns of their critics. As Abbott notes:

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[134] J. Ordover and R. Willig, "Department of Justice Merger Guidelines: An Economic Assessment," (1983) 71 C.L.R. 535 California Law Review.

[135] J.D. Pace, "The Changing Role of Supply Substitutability in Defining and Measuring Relevant Markets," New Merger Guidelines ed. J. Schenefield, Practising Law Institute, Course Handbook, No. 397 (1982), 103, at pp. 114-115.

> As the 1984 Guidelines indicate, the mere presence of imports indicates next to nothing about the ability of foreign producers to constrain the exercise of market power by domestic producers.[136]

The author proceeds to list eleven factors which he contends are crucial in determining the relevant market,[137] while contemporaneously elevating import restrictions to a predominant position.

> In general, these factors bear on the price elasticity of foreign supply and domestic demand, elements that are crucial in determining the scope of the geographic market.[138]

Import restrictions are subdivided into the two principal classifications, tariffs and quotas. Tariffs, according to Abbott, do not alter the general premise advocated by Landes and Posner:

> In sum, it is almost never appropriate to cite the existence of a specific or ad valorem tariff as grounds for significantly discounting foreign market shares,

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[136] Supra, n. 123, at p. 317.

[137] Ibid., "In determining whether the producers who are responsible for imports should be included in the relevant market, the following factors must be considered: (1) the nature of import restrictions; (2) product differentiation; (3) other barriers to entry; (4) transportation costs; (5) foreign and domestic price correlations; (6) shipment patterns; (7) exchange rate patterns; (8) contractual terms; (9) portfolio diversification by buyers; (10) the degree of firm integration; and (11) foreign conditions of production.

[138] Ibid., at p. 329.

> assuming import penetration already exists.[139]

In contradistinction, quotas restrict the degree to which foreign competition is able to dampen domestic market power. If a fixed-quantity quota exists, the market share of foreign firms should be reduced to the level of actual imports, with the value of the quota acting as an upper bound.

> Unlike tariffs, under which foreign supply price elasticity remains positive in response to a domestic price increase, fixed-quantity quotas yield a foreign supply price elasticity equal to zero.[140]

On the other hand, a fixed-percentage quota creates a negative foreign supply response to a domestic price increase.[141] It is submitted that, in general, a rebuttable presumption should operate to include all foreign market shares based on capacity or sales in the relevant market. This presumption could be rebutted by the applicant, and the weight accorded foreign market shares could be diminished proportionately, on proof of a low foreign import price elasticity. To this extent, the "five percent" market share test proposed in section 2.4 of the 1984 Guidelines is consistent and acceptable.[143]

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[139] Ibid., at p. 319; Abbott, at p. 317: "If imports already are present in the market the existence of a specific tariff (stated in terms of the number of dollars per unit sold) or an ad valorem tariff (stated as a percentage of the sales price) will not significantly constrain the rate of foreign supply response - and, thus, should not be used to discount the market shares assigned existing foreign producers. A tariff merely "shifts up" the marginal cost curves of foreign firms. (A specific tariff shifts marginal cost curves up and to the left by a constant amount, while an ad valorem tariff shifts up and increases the slope of foreign producers' marginal cost curves.) Accordingly, foreign supply elasticity remains positive under a tariff - foreign producers are able to constrain significant domestic price increases by raising their rate of exportation and thereby bringing additional imports into the domestic market."

[140] Ibid., at p. 319.

[141] As domestic prices increase and output decreases, imports will fall as a result of the fixed-percentage quota. Consequently, foreign market shares should be assigned values less than those resulting from existing importation levels.

(e) The Relevant Geographic Market And Supply Substitutability

The relevant product market defines all production and sales, or capacity, that could reasonably be included or diverted into producing the relevant product and would mitigate the potential market power of the merging firm, assuming transportation costs are negligible. The simultaneous super imposition of the geographic market circumscribes the relevant product market in an effort to include only those firms which will potentially compete with the merging firm if transportation costs are non-negligible. In effect, the delimitation of the geographic market is establishing the location of the sellers, not the buyers, who may potentially impede the merging firms's market power. The geographic markets of the two merging firms must at least intersect in order for the merger to raise horizontal merger concerns.[143]

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[143] See: supra, n. 1, at section 2.4: "If shipments from a particular country to the United States are subject to a quota, the market shares assigned to firms in that country will not exceed the amount of shipments by such firms allowed under quota." See also: supra, n. 1, at section 2.34: "Although voluntary or involuntary quotas may prevent foreign competitors from increasing their imports into the United States in response to a domestic price increase, The Department will not exclude foreign competitors from the relevant market solely on the basis of the quotas. This is primarily because it frequently is difficult to determine and measure the effectiveness and longevity of a particular quota or any offsetting supply response from firms in countries not subject to the quota. The Department will consider the effects of a quota as a separate factor in interpreting the significance of market shares and market concentration. See Section 3.23 (Special Factors Affecting Foreign Firms.)"

The settlement of the geographic market boundaries parallels the delineation of the product market; seven essential issues have previously been considered in outlining the product boundary:

(1) The provisional market,

(2) Geographic substitutability,

(3) Other relevant factors,

(4) Price discrimination,

(5) Product differentiation,

(6) Calculation of market shares, and

(7) Foreign competition.

Apart from price discrimination which is necessary in defining the relevant product, similar rubrics are recruited to structure the characterization of the relevant geographic market.

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[143] Non-intersection of the two merging firms' geographic market gives rise to contemplation of "segmented markets." See: Werden, supra, n. 86.

First a provisional geographic market is established by analyzing the existing shipment patterns of the merging firm and its closest competitors. As a rule of thumb, this provisional market will encompass an area in which the merging firm makes a significant percentage of its sales,[144] while firms outside the area account for a small percentage of the sales.[145]

The provisional geographic market will then be expanded to include all other firms which could easily and economically shift their sales to the provisional market due to a "small but significant and nontransitory" increase in the price of the relevant product in the course of one year.[146] The intent of including geographic substitutability is to broaden the market beyond the seller's area of operation due to the fact that market power inside the provisional market is bounded by potential rivals outside the area.[147] One must recall that the "diversion" theory proposed by Landes and Posner would require the total production and sales, or capacity, of the outside firm to be included in the market, unless the product is subject to price discrimination (or government imposed barriers to entry). The DOJ will continue to annex the location of the outside firms until,

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[144] This is a codification of the "LOFI" doctrine - "little out from inside.

[145] Similarly, this enunciates the "LIFO" principle - "little in from outside." The principles of "LIFO" and "LOFI" are frequently referred to as the "shipments tests." This test was explored in great depth by Elzinga and Hogarty. "The Problem of Geographic Market Delineation in Antimerger Suits," (1973) 18 Antitrust Bulletin 45. In addition, Werden, supra, n. 86, at p. 578 compares and contrasts the 1982 Guidelines and the "shipments test".

[146] In addition, the barrier to entry problem is discussed further at 4493.30, s. 3.3.

> the Department identifies an area in which a hypothetical monopolist could profitably impose a "small but significant and nontransitory" increase in price. The "smallest market" principal will be applied as it is in product market definition. Both the price in which an increase will be postulated and what constitutes a "small but significant and nontransitory" increase in price will be determined in the same way in which it is determined in product market definition.[148]

As in the case of defining the relevant product market, the critical difficulty with the "five percent test" is to predict the possible shifts in supply due to a hypothetical price increase. To assist, the DOJ will infer the likely effects of a price increase from all reliable circumstantial evidence including:[149]

(1) The shipment patterns of the merging firm. It is

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[147] See: D.I. Baker and W. Blumenthal, "The 1982 Guidelines and Existing Law," (1983) 71 Columbia Law Review 311, for a review of supply substitution and the geographic market outlined in the 1982 Merger Guidelines.

[148] 1984 Guidelines, supra, n. 1, at 4492.301, s. 2.31.

[149] 1984 Guidelines, supra, n. 1, at 4492.302, s. 2.32.

submitted that this element is determinative of the provisional market, not its expansion.

(2) Evidence of buyers actually shifting to other geographic areas, especially due to changes in relative prices. It is submitted that this observation is misplaced; it implies demand rather than supply substitutability.

(3) If transportation costs are not a significant percentage of the final price, the inference may be drawn that the outside supplier may have a higher propensity to shift sales into the provisional market.[150]

(4) If local distribution costs are low, again one may infer that the geographic substitution response would be higher.

(5) Finally, the DOJ may deduce from a high level of excess capacity exhibited by the outside firms that barriers to entry do exist. The discussion regarding barriers to entry, infra, casts much doubt on this argument. It is quite possible that the incumbent firms are extremely efficient.

Although some commentators criticize the basic procedure outlined above for delineating the geographic boundary,[151] it is recommended that such a flowchart of issues in the Canadian context is desirable for consistency, clarity and continuity.

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[150] Applying the "diversion" principle, if the outside firm is making any sales in the provisional market, the level of transportation costs is immaterial.

The fourth parameter which may influence the imposition of market power in a geographic area is the ability of the merging firm to price discriminate. Analogous to the case of product market definition,

> the Department will consider defining additional, narrower geographic markets consisting of particular locations in which a hypothetical monopolist could profitably impose a "small but significant and nontransitory" increase in price.[152]

As Werden remarks:

> In the foregoing procedure, the postulated price increase is a uniform increase in each seller's factory-gate price. The Guidelines' market delineation procedure initially assumes that there is no price discrimination and that market power, if it exists, would therefore be exercised through a uniform price increase. However, if price discrimination is possible, market power can be exercised selectively against only the most vulnerable groups of consumers. Under these circumstances, the Guidelines permit the delineation of additional, narrower...markets.
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> . . . .

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[151] For a general compilation of relevant articles, see: "Symposium: 1982 Merger Guidelines," (1983) 71 California Law Review 281. In particular R.G. Harris and T.M. Jode, "Market Definition in the Merger Guidelines: Implications for Antitrust Enforcements," (1983) 71 California Law Review 464, recommend a reverse onus on the defendant, in a private action, to expand the market on proof of "hard" evidence.

[152] 1984 Guidelines, supra, n. 1, at 4492.303, s. 2.33.

> Although all markets are delineated by applying the Guidelines' definition of a market to areas and groups of products, the possibility of price discrimination significantly alters the analysis. Rather than postulating a uniform increase in factory-gate prices, markets are delineated by postulating a discriminatory price increase applied only to particular customers.[153]

Moreover, following the procedure formulated for the product market, geographic market shares will be calculated on the basis of capacity figures, unless sales figures more appropriately manifest the deterrent effect on market power for differentiated products. In general, capacity, rather than sales is a more reliable measure of market power because it includes the potential modification of production.[154]

Penultimately, foreign competition and its effects on competitive performance in the domestic market is treated with the acknowledged deference granted in defining the relevant product market. If the outside firm is merely a national firm which has not been included in the provisional geographic market, then no special rules apply. However, if the outside firm is extraterritorial, then international business factors are considered.[155] As discussed above,[156] the general premise is to treat foreign and domestic firms identically. Consequently, potential rivalry from foreign competitors is contemplated and examined in much the same fashion as any potentially competitive rival.

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[153] Werden, supra, n. 86, at p. 529.

[154] See: United States v. Amax, Inc., 402 F.Supp. 956, 961 (D.Conn. 1975).

[155] 1984 Guidelines, supra, n. 1, at 4492.303, section 2.34. Exchange rates, tariffs, quotas and political conditions will be included in the analysis.

[156] Supra, n. 142, and accompanying text.

Finally, the market share is calculated on the *likelihood* that sales are to be made or capacity is to be used due to the requisite price increase. This concluding step adjusts the market boundaries for such restrictions as prior contracts committing present capacity or the existence of excessive transportation costs.[157]

In a simplified format, the 1984 Merger Guidelines establish, from the consumer's perspective, the set of products that are interchangeable and reasonably substitutable, and label this related set the relevant product. Next, the Guidelines endeavour to prescribe the array of firms that would expediently and inexpensively shift their current output or capacity to the production of the relevant product in reaction to a "small but significant and nontransitory" increase in the price of the relevant product. This resulting cluster of *output* is referred to as the relevant product market. Alternatively, the number of firms profiled by the "outer boundary" of the geographic market constitutes the relevant product market. The final issue investigates whether all of these firms would realistically constrain the exercise of market power by the merging firm. Stated equivalently, the relevant product market is abridged or truncated to include only the subset of firms which would ship into the merging firm's provisional geographic market due to an hypothetically predefined price increase. Eventually, the relevant market, which defines the denominator of the market share statistics, emerges from the superimposition of the relevant geographic market onto the relevant product market.

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[157] See: J.A. Ondover and R.D. Willig, "The 1982 Department of Justice Merger Guidelines: An Economic Assessment," (1983) 71 *California Law Review* 535, for technical criticisms of the 1984 Guidelines' market definition and measurement. The authors praise the inclusion of the "provisional market" concept.

(f) Relevance Of The Relevant Market In Canadian Merger Policy

It is almost presumptuous to underscore the fundamental reliance of the 1984 Merger Guidelines on the condition precedent of market definition. Any structural test of market power which employs market shares as an independent variable is extremely sensitive in its policy impact to variations in the size of the market. If the market is defined too broadly, then the concentration measure will underestimate the market power resulting from a potential merger; alternately, if the market is unjustifiably restricted, then the structural measure of market power will overestimate the anticompetitive effect of the merger. As is being suggested in this paper, if the HHI is used to monitor market power, a realistic estimate of the bounds of the relevant market is indispensible in order to properly track market power.

An exhaustive comparison of the 1984 Merger Guidelines with the seminal work by Landes and Posner[158] must lead one to the inevitable observation that the DOJ adopted the fundamental precepts of the authors' propositions. Supply substitution is given new significance; geographic substitution is similarly elevated to a position of consequence. Secondly, demand and supply shifts are constructed from a small but significant hypothetical price change above the current price level.[159] In addition, other factors are considred to predict the likely effect of increased future prices on market elasticity of demand.[160] Landes and Posner also recommended procedures for amending the market in the light of price discrimination[161] and product differentiation,[162] procedures which were adopted by the DOJ. Moreover, foreign competition is presumptively treated in an identical fashion to domestic competition.[163] The 1984 Guidelines' approach to market measurement and their emphasis on the inclusion of the total capacity of potential competitors can be nothing less than a blanket adoption of the "diversion principle."[164] In sum, the 1984 Merger Guidelines are formulated on the predicted correlation between market power and firm elasticity of demand, accompanied by *ex ante* adjustments to market delineation, concepts advocated by Landes and Posner.

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[158] Landes & Posner, supra, n. 8.

[159] Not the competitive price level as some commentators propose. See D.I. Baker and W. Blumenthal, The Revised Merger Guidelines: One Step Forward, Two Steps Back," Legal Times, July 9, 1984, p. 34.

[160] See: equation (3), supra. The 1984 Guidelines are addressing the issue of modifying the market for demand and supply elasticity. See: Landes & Posner, supra, n. 8, at p. 945.

[161] Supra, n. 8, at p. 965.

[162] Landes & Posner, Ibid., at p. 967.

The Canadian courts appear to minimize the policy relevance of systematically and methodically defining, in a particularized detailed fashion, the pertinent product and geographic markets. Specifically with respect to the matters of supply substitution and potential competition, the leading merger cases all but ignore the issues entirely. In the Canadian jurisprudence, demand substitutability is addressed at the market delineation stage, while supply substitution is, at best, impliedly contemplated when market shares are adjusted for existing barriers to entry. In contrast, the 1984 Guidelines envision a determination of both at the preliminary market designation stage. Because it requires the courts, or the Director, to determine the issue explicitly, it is submitted that the latter method is preferable.

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[163] *Ibid.*, at p. 966.
[164] *Ibid.*, at p. 963.

Three merger cases, which on the first blush might possibly have established persuasive precedent, have come before the Canadian courts.[165] In the *Canadian Breweries* case, the accused was charged under the former combine section[166] of embarking on a policy of acquiring competing companies engaged in the production and distribution of beer. By 1958, the accused controlled sixty percent of the central Canadian market, a large proportion of the Western market, and only a relatively small share of the Maritime market. Section 2(e) of the former *Combines Act* defines a merger as one or more persons,

> (i) who has or have purchased, leased or otherwise acquired any control over or interest in the whole or part of the business of another, or
>
> (ii) who either substantially or completely control, throughout *any particular area* or district in Canada, or throughout Canada *the class or species of business* in which he is or they are engaged, [emphasis added]
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> and extends and applies only to the business of manufacturing, producing, transporting, purchasing, supplying, storing or dealing in commodities which may be the subject of trade or commerce; but this paragraph

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[165] *R.* v. *Canadian Breweries Ltd.* (1960), 34 C.P.R. 179, 126 C.C.C. 133, [1960] O.R. 601; *R.* v. *British Columbia Sugar Refining Co. Ltd. and B.C. Sugar Refinery Ltd.* (1960), 38 C.P.R. 177, 129 C.C.C. 7, 32 W.W.R. 577; *R.* v. *K.C. Irving Ltd. and 3 other Corporations*, [1978] 1 S.C.R. 408, 32 C.C.C. (2d) 1, 29 C.P.R. (2d) 83, 15 N.B.R. (2d) 450 (Appeal to S.C.C.).

[166] S.32(1) and S.2(e) of the Combines Act, R.S.C. 1952, c. 314, prior to the 1960 amendments.

> shall not be construed or applied so as to limit or impair any right or interest derived under the Patent Act, or under any other statute of Canada.[167]

This definition certainly contemplates the elements of a product and geographic market. However, McRuer C.J.H.C., does not explicitly address the matter of market definition. Regarding the relevant product market, McRuer C.J.H.C., by noting the allegations of the Crown, appears to assume that the relevant product is beer,

> (i) Creating barriers to the entry of new competition in the brewing industry [emphasis added].[168]

There is no allusion or implicit recognition of demand substitution in the entire judgment. Furthermore, the incorporation of supply substitution to aid in the determination of the relevant product market is completely disregarded. With regard to the geographic boundaries, again no express determination of the issue is proffered. The reader is left to presume that the market is provincial from such indirect references as:

> The share of the market enjoyed by the accused in Ontario rose from 11.2% in 1931 to 60.9% in 1958.[169]

and,

> It requires no exhaustive analysis of the constitutional authorities to state that each Province has jurisdiction to regulate and control the sale of liquor within its boundaries and to fix the prices at which, and the conditions under which liquor may be

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[167] Ibid., section 2(e).
[168] Supra, n. 165, at p. 141.
[169] Ibid., at p. 144.

> sold.[170]

and,

> Specific evidence was introduced to support the allegation that the Brewers' Warehousing Co. Ltd. was used as an instrument to exclude from the Ontario market the products of breweries with plants outside of Ontario.[171]

It is noteworthy that the court does recognize the influence of foreign competition:

> It may well be that the members of the Brewers' Warehousing Co. Ltd. do use this company to make it difficult for foreign competitors to enter the market, but it is using a wide net in a criminal case to hold that this flows from the merging of the companies that constitute the accused.[172]

Although McRuer C.J.H.C., makes reference to the "market" on numerous occasions, one must conclude that a systematic determination of the relevant product and geographic boundaries is absent.

In the second merger prosecution in 1960, Williams C.J.Q.B., in the B.C. Sugar case, also neglects to define the relevant market. Williams C.J.Q.B. refers only tangentially to the relevant product as sugar:

> The price of the product in question in this prosecution, sugar, is not so controlled.[173]

Although the court presumed that cane and beet sugar were fungible, no attention was given to the demand substitutability between sugar and other close substitutes such as saccharin:

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[170] Ibid., at p. 145.
[171] Ibid., at p. 154.
[172] Ibid., at p. 154-5.
[173] Supra, n. 165, at p. 24.

> The importance of this cane/beet differential is apparent. Not only has it the effect of reducing the price of beet sugar, but it exists, as counsel for the accused pointed out, "for strictly competitive reasons". It is a definite element in competition. The evidence satisfies me that there is always a very real competition between cane and beet sugar. If no such competition existed there would obviously be no cane/beet differential; there would be no need for it.[174]

The logic of the foregoing deduction is certainly suspect; the fundamental issue should contemplate substitution at identical prices. Earlier in the judgment, Williams C.J.Q.B. intimates that consumer preference may exist between the two:

> "The selling price of refined beet sugar at a particular point is the refined cane sugar price at that point. In some circumstances, however, particularly in localities where the consumer shows a strong preference for cane sugar, it has been the practice to allow a discount or differential on the price of beet sugar. This is termed the cane/beet differential.[175]

The court appears to be accepting beet and cane sugar as substitutes because the beet/sugar price differential remains relatively stable over time:

> "Thus, the sale price of beet sugar never exceeds that of cane sugar and is usually less. Any change in the selling price of cane sugar will almost automatically result in a corresponding change in the selling price of beet sugar by reason of the selling price of beet sugar being directly governed by the price of cane sugar.[176]

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[174] Ibid., at p. 63.
[175] Ibid., at p. 38.
[176] Ibid., Note that the 1984 Guidelines contemplate this factor in section 2.12.

The court does make mention of the inelasticity of demand,

> It was also accepted that the price of sugar is no real deterrent to the sale of sugar unless the price gets too far out of line.[177]

But, there does not exist anywhere in the judgment a correlation between the degree of elasticity and market shares or market power. Furthermore, it is not clear how the possible substitutability betwen cane and beet sugar operates to influence either market shares or market power.

The matter of supply substitution is analyzed, not from the perspective of market definition, but from the viewpoint of ex post adjustment of market power.[178] As Williams C.J.Q.B. states:

> Apparently no one else manifested a real desire at any time to enter the sugar refining business in British Columbia or Alberta. There may have been many reasons, probably all economic, why this was not done. It was open, and is still open, to any one to do so.
>
> . . . .
>
> It was admitted, in the course of these discussions, that there was and is always the likelihood of competition in the four Western Provinces, although it was said that such competition was "pretty remote when you come to Manitoba because of the freight". This discussion was primarily directed to offshore competition from the West Coast. The likelihood of offshore competition from the East Coast also exists and has always existed and was and is not remote in Manitoba "because of the freight". Until the Manitoba Company began to refine beet sugar, the sugar sold in

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[177] Ibid., at p. 36.

[178] Williams C.J.Q.B. appears to be evaluating the degree of entry barriers. The issue of present firms shifting their operations into sugar refining is not addressed, although this oversight may be inconsequential.

> Manitoba was largely Eastern refined cane sugar.
>
> Of course the merger complained of had nothing to do with the situation existing before it came into effect. After the merger the accused owned the only producing refinery in Manitoba. There is nothing that I can see to prevent others, including the Eastern refiners or some of them, entering the field of sugar refining in Manitoba at any time. There would seem to be no economic reason, except, perhaps, the effects of over-production, to prevent them.[179]

The foregoing excerpts also embody elements of geographic substitutability; however, it is submitted that the fundamental economic test has been neglected. The issue is not whether conversion, expansion, or new entry is likely to occur at the current price level, but whether an increase in price due to augmented market power will induce such production substitution.[180]

In the leading Supreme Court of Canada decision on section 33, Combines Investigation Act, 1976, Laskin C.J.C. writing per curiam, appears to adopt the definition of the relevant market established by Robichaud J. at trial. The relevant product market is impliedly accepted as English language daily newspapers. As Laskin C.J.C. notes in obiter:

> Limerick, J.A., made a point, however, of separating the newspaper as a physical object, consisting of pages of newsprint, from the expression of ideas therein, its editorial comment and the editing of news; and he held that although as a physical object a newspaper was caught by the combines legislation as being an article

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[179] Supra, n. 94, at pp. 61-62.

[180] It is never completely clear in the judgment whether the geographic market is the province, Western Canada, Canada or the international setting.

> of trade or commerce, the legislation would not cover the contents as such. This is not a question that I need decide here and I leave it open, especially in view of the fact, established by the evidence, that editorial control of the five newspapers was left in the hands of their respective publishers and editors without any attempt at central or other combined direction.[181]

With respect, a designation that the relevant product market is news or advertising in contrast to newspapers, would significantly alter the market boundaries, acknowledge demand substitution, and inevitably alter the determination of monopoly power. In contrast, the geographic market is delineated by the Court in a manner strikingly similar to the procedure recommended for determining the "provisional" geographic market in the 1984 Guidelines:

> It was common ground that New Brunswick was the proper market area within which to assess the existence of a prohibited merger or monopoly. There was no significant circulation of any of the New Brunswick newspapers outside the Province and, correlatively, there was no significant circulation within New Brunswick of newspapers published elsewhere; the latter constituted about three per cent of newspaper circulation in the Province.[182]

Apparently adopted by the Supreme Court of Canada, the rationale for defining the relevant market as English language newspapers in the province of New Brunswick is found in Mr. Justice Robichaud's judgment at trial.[183] Mr. Justice Robichaud reviews several Canadian cases in order to ascertain the meaning of "relevant market" in terms both of commodity and geography. In the Canadian Breweries case,[184] Robichaud J. notes that:

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[181] Supra, n. 165, at p. 5 (S.C.C.).

[182] Ibid., at p. 6. Note that the "LOFI" and "LIFO" rules of thumb are applied by Laskin C.J.C.

[183] Supra, n. 165, at p.71 (Trial).

> Nowhere in that case, as submitted by the Crown herein, did defence counsel raise the argument that beer did not constitute a market because it was part of a larger market for alcoholic beverages or for beverages generally.[185]

Although some judicial pronouncements have been made in non-merger cases, the issue of relevant market is still applicable to the merger situation. In R. v. Burrows et al. [186] the court held that mandarin oranges, although a small proportion of the orange market, the citrus market and the food market, constituted a separate market. Mr. Justice Gibson, in the Coat and Apron case, makes reference to the concept of the submarket:[187]

> It is obvious that a Court may be required to exercise a judgment on the evidence on whether the market specified in the indictment or the particulars, of which proof is accordingly made, has not been artificially limited to suit the available evidence. On the other hand, where a charge is made in respect of a market area which is broader than need be to sustain it, the Crown will not fail if it does not establish an agreement referable to the whole of the area; it is enough if it adduces evidence referable to an acceptable competitive market within that defined in the indictment; and, it may do that by evidence which, although not addressed to each section or unit of the competitive area (if it can be thus fragmented) will

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[184] Supra, n. 165.

[185] Supra, n. 165, at p. 76 (Trial).

[186] R. v. Burrows et al. (1966), 54 C.P.R. 95.

[187] See: Brown Shoe Co. v. U.S., 370 U.S. 294 (1962), discussed at n. 77, supra. This concept also appears to justify the narrow market accepted in Burrows.

> none the less support an inference that the market scope of the illegal agreement is that comprehensive.'[168]

With respect, it is not abundantly clear how the Court determines the "acceptable competitive market". Furthermore, the concept of fragmenting the market into sections or units may raise the sectre of the "segmented market" problem; the proscribed conduct must offur in the *same* market. Following this review of the Canadian case law pertaining to market definition, Robichaud J. acknowledges a list of pertinent characteristics which may be helpful in delimiting the relevant market developed by Gibson J. in the *J. W. Mills* case.[169]

The defence, in an effort to broaden the market, argued that the relevant product was not English daily newspapers:

> In support of the last-mentioned ground, defence counsel dealt at some length with the *"competition between daily newspapers and radio and TV."*[170]

Mr. Justice Robichaud rejects this contention on the grounds that the newspapers in question are in competition:

> His conclusion, therefore, that the above two newspapers "are complementary rather than competing

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[168] *R.* v. *Canadian Coat & Apron Supply Ltd. et al.* (1967), 52 C.P.R. 189, [1967] 2 Ex.C.R.53, 2 C.R.N.S. 62, at p. 59 C.P.R.

[169] *Supra*, n. 165, at p. 78-79 (Trial). These concepts were developed by J. Gibson in the *Mills* case. Appeal to S.C.C. dismissed. See: *R.* v. *J.W. Mills & Son Ltd. et al.* (1968), 56 C.P.R. 1, [1968] Ex. C.R. 275; affd 64 C.P.R. 7, 1, C.C.C. (2d) 420, 14 D.L.R. (3d) 464, at p. 35.

[170] *Supra*, n. 165, at p. 70 (Trial).

> newspapers" is wrong. It is against the evidence viewed as a whole, particularly so if I consider, as I must, the statement made by no less than Mr. Ralph Costello, in a letter dated December 7, 1962, addressed to Brigadier Michael Wardell, the then publisher of the Fredericton "Gleaner": "The fact is, in Saint John and Moncton *we think of you (with your Gleaner and Advocate) as a pretty tough competitor*, and there undoubtedly will be days when we would find it difficult to promote your publications."[191]

Note that the court is basing demand substitutability on seller perceptions, a concept which, as discussed *supra*, is suspect.[192]

The geographic boundaries are established by relying on buyers' perceptions, a factor which by itself is less than credible.[193] As Robichaud J. concludes:

> Another basic proposition which I am adopting is a further submission, of the Crown.
>
> > The Province of New Brunswick is a separate political entity. As such it necessarily generates news of particular interest to its inhabitants and of less direct interest to others. Many, perhaps most, of the laws that affect the citizen in his daily life are provincial laws administered by provincial officials. The courts are provincial institutions. Public utilities are supervised by the province. Education is a provincial matter. Virtually all taxes except the Federal income tax are provincial matters. So are health care and welfare and innumerable other facets of life which concern all or most citizens. In short the news about most of the matters of direct and immediate concern relates to provincial activities.

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[191] *Ibid.*, at n. 165 (Trial).
[192] See: 1984 Guidelines, *supra*, n. 1, at 4492.102, 2.12.
[193] See: 1984 Guidelines, *supra*, n. 1, at 4492.302, s. 2.32.

> May I add that, in order to shorten my own remarks, I am accepting the reasoning of Crown counsel, in his brief, as well founded on the factual evidence herein.
>
> I therefore am satisfied, beyond a reasonable doubt and find, as a fact, that geographically, the Province of New Brunswick is the relevant market for its five English-language daily newspapers.[114]

The analysis of the "relevant market" in the K.C. Irving case is commendable for several reasons. First, the courts have accepted the bipartite reconstruction of the market into the hypothetical product and geographic markets. Second, product substitutability was acknowledged. And finally, the courts have appeared to recognize the interdependent determination of the "provisional" geographic market based on the doctrines of "LIFO" and "LOFI".

Unfortunately, the issues addressed and the determining factors chosen seem to be coincidental at best and random at worst. The fundamental concept of buyer shifts due to a small but significant price increase of the provisional product does not surface in the jurisprudence. The corresponding concept of supply substitution and potential competition have been noticeably and improperly neglected in the entire realm of Canadian case law development. In addition, the geographic market should not be constrained to the provisional market; geographic substitutability should permit a broadening of the initial market to include all significant market power deterrance. If one theme need be chosen for improvement in the Canadian adjudicative context, it is submitted that production and geographic substitution is by far the number one candidate.

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[114] Supra, n. 165, at p. 79 (Trial).

Less obvious concerns must also be recognized by the adjudicative body. To highlight a few, price discrimination, product differentiation, the appropriate measure for market shares and the diversion principle must all be evaluated in an effort to define the appropriate market boundaries. The entire analysis must endeavour to ascertain the appropriate market in which the merging firm could exhibit market power.

The proposal to adopt Canadian guidelines similar in structure and scope to the American 1984 Guidelines, at least in so far as they pertain to relevant market delineation, must not be perceived as being tantamount to recommending a step-by-step recipe for use by the adjudicative body. It is of utmost importance to recall that the guidelines are directed for use by the Director, not the Competition Tribunal or the courts. The object of reviewing the Canadian jurisprudence has been to highlight that guidelines adopting the generally accepted precepts of market delineation would be neither inconsistent with nor more restrictive than prevailing judicial pronouncements. Arising from the employment by the Bureau of Competition Policy of such a "merger manual", a salutory spinoff might be the avoidance of judicial myosis when reviewing the process of relevant market delineation.

C HORIZONTAL MERGERS

1. INTRODUCTION

Once the relevant market has been determined and the measurement of the resultant market shares finalized, the chosen test for concentration is applied and evaluated. The 1984 Guidelines[1] have selected the HHI to measure the correlation between the existent level of concentration and the two targeted independent variables of predominant significance, the number of firms in the market and their respective shares. As the 1984 Guidelines acknowledge:

> Markets can range from atomistic, where very large numbers of firms that are small relative to the overall size of the market compete with one another, to monopolistic, where one firm controls the entire market. Far more common, and more difficult analytically, is the large middle range of instances where a relatively small number of firms account for most of the sales in the market.[2]

Unfortunately, the conceptual criticisms surrounding the application of the HHI to measure market power arise in this "large middle range of instances". The DOJ assumes that an increase in market concentration inevitably leads to an increase in market power and a decrease in the number of firms increases the predeliction for collective action.

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[1] All subsequent references to the Merger Guidelines in this section are as follows:
1968 Merger Guidelines, CCH Trade Reg. Rep., par. 4510.
1982 Merger Guidelines, CCH Trade Reg. Rep., par. 4500.
1984 Merger Guidelines, CCH Trade Reg. Rep., par. 4490.

[2] Supra, n. 1, at par. 4493.10, s. 3.1, note 13.

> Other things being equal, concentration affects the likelihood that one firm, or a small group of firms, could successfully exercise market power. ... If collective action is necessary, an additional constraint applies. As the number of firms necessary to control a given percentage of total supply increases, the difficulties and costs of reaching and enforcing consensus with respect to the control of that supply also increase.[3]

It is interesting to note that the 1984 Guidelines endeavor to employ both the "dispersion" theory of oligopolistic behaviour conjunctively with the "collusion" hypothesis. In sum, the 1984 Guidelines presume a decrease in the number of firms or the equality of market shares leads to an increase in the HHI and the level of concentration, ultimately resulting in the deduction that competition has diminished. Although the inference of high concentration from large values of the HHI may be questionable, and similarly the correlation between concentration and market power suspect, the 1984 Guidelines accept the general premise of a determinable causal link between the HHI, concentration and market power. As the 1984 Guidelines insist:

> Unlike the traditional four-firm concentration ratio, the HHI reflects both the distribution of the market shares of the top four firms and the composition of the market outside the top four firms. It also gives proportionately greater weight to the market shares of the larger firms, which probably accords with their relative importance in any collusive interaction.[4]

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[3] Ibid.

[4] Ibid.

Generally, the 1984 Guidelines may be perceived as an extensive and coherent compilation of the "state of the art" concepts respecting the economics of mergers. The great "economics takeover" of the past decade has been abridged and digested into a set of antitrust merger rules that are economically justifiable, legally practical and politically acceptable. As Donald J. Baker, former assistant attorney general in the American Antitrust Division of the DOJ asserts:

> By contrast, William Baxter's new guidelines are as much an economic essay on the Antitrust Division's thinking process as they are a specific guide to conduct. They set forth in great detail the economic policy on which the department is now bringing cases.[5]

The overview of the treatment of horizontal mergers contained in the 1984 Guidelines[6] presented below is segmented into five aspects. First the test for concentration is reviewed and evaluated. Second, the qualitative factors embodying an immensely broad scope of economic theory are acknowledged; it is submitted that these factors form the foundation of the 1984 Guidelines. An indepth perusal and critical appraisal of the qualitative variables would be imperative prior to the adoption of this section of the American guidelines to the Canadian case. Even as the DOJ readily admits:

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[5] Donald J. Baker, "Merger Guidelines Viewed as an Essay on Economics", June 24 (1982) 187 New York L. J.19.

[6] For a general discussion of the 1982 or 1984 Merger Guidelines, see: Elanor M. Fox, "The New Merger Guidelines: A Blueprint for Economic Analysis", (1982) 27 Antitrust Bulletin519; John E. Scarborough and Malcome R. Pfunder, "New Merger Guidelines Not Always Less Restrictive", January 10 (1983) 5 Legal Times19; James M. Johnstone and Gene C. Schaerr, "Retooling the Merger Guidelines", May (1983) 69 American Bar Assoc. J.584; W. F. Baxter, "A Justice Department Perspective", (1982) 51 Antitrust L. J.287; Paul Pautler, "A Review of the Economic Basis for Broad-Based Horizontal-Merger Policy", (1983) 28 Antitrust Bulletin571; John Kwoka, "Antitrust Analysis and the Cooperating Core: It's the First Two Market Shares that Count (II)", (1984) 16 Antitrust Law and Economic Rev. 47.

> However, market share and concentration data provide only the starting point for analyzing the competitive impact of a merger. Before determining whether to challenge a merger, the Department will consider all other relevant factors that pertain to its competitive impact.[7]

The third area attempts to emphasize the general trent in American antitrust thinking by comparing the 1982 and 1984 Guidelines.

Fourthly, the override provisions of the leading firm proviso are outlined. Understanding of the intent of the guidelines would be incomplete without consideration of the changes culminating in the 1984 version of the Merger Guidelines. Finally, several concluding remarks are offered with the prospect of accommodating the American administrative guidelines to the Canadian injunctive proceedings under the Competition Act.

2. MEASUREMENT OF CONCENTRATION THRESHOLDS

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[7] Supra, n. 1, at par. 4493.101, s. 3.11.

(a) The Test

The DOJ artificially divides the entire array of possible concentration levels into three categories defined by the post-merger level of the HHI in the relevant market. The lowest level of concentration, the unconcentrated market, is bounded by a HHI less than 1000. Within this "safe harbour", the DOJ will not challenge a merger of any size except in "extraordinary circumstances".[8] The second stratum of concentration, the moderately concentrated market, is defined by a HHI level within the range 1000 to 1800. The highly concentrated market exhibits a HHI exceeding 1800. The HHI thresholds of 1000 and 1800 correspond to mean CR4 levels[9] of 50 and 70 percent respectively. Economic analysis should be undertaken to determine comparable or acceptable thresholds for the Canadian economy. As a general principle, the higher minimum efficient scale of firms and the propensity for efficiency consideration in Canada will undoubtedly elevate the threshold levels beyond the American standards. Moreover, the tailoring of the 1984 Guidelines to provisional relief should also pressure the thresholds upwards with the objective of capturing indisputably objectionable mergers.

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[8] See: 1984 Guidelines, par. 4493.101(c), s. 3.11(c). Under the 1982 Guidelines, the DOJ was simply "unlikely" to challenge (par. 4503.101(c)). In addition, no guidance is offered on what may be treated by the DOJ as an "extraordinary circumstance".

[9] See the discussion supra, Chapter VIII E, on mapping the CR4 into the HHI.

The DOJ, in evaluating horizontal mergers, will consider "the post-merger market concentration and the increase in concentration resulting from the merger".[10] Assuming the HHI properly tracks concentration, the sum of the squares of the market shares combined will be greater than the squares of the market shares of the individual merging firms summed.[11] Specifically, the increase in the HHI as a result of the merger will be equivalent to twice the product of the market shares of the two merging firms. Alternatively, the change in the HHI is monitoring the size of the merging partners. The 1984 Guidelines presuppose that not only the degree of concentration within the market, but also the relative size of the firms concerned, is instrumental in determining whether the merger facilitates the acquisition of market power. Indispensable to this proposition is the recognition that the merger increases concentration. This deduction is only guaranteed if the relevant market has been previously delineated correctly, particularly with respect to supply substitutability.

In a moderatly concentrated market, the DOJ is "likely" to challenge a merger which gives rise to an increase in the

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[10] Supra, n. 1, at par. 4493.101, s. 3.11.

[11] See: Discussion, supra, on the HHI. See also: 1984 Guidelines, supra, n. 1, at note 15.

HHI of greater—than 100 points *unless* the Department concludes "that the merger is not likely substantially to lessen competition".[12] This exception is based on a finding by the DOJ that there is the presence of other qualitative factors enunciated in sections 3.2 to 3.5.[13] The similarity in wording of the exclusion clause to the substantive provisions in the Canadian Competition Act cannot be disregarded; the qualitative factors in the 1982 Guidelines may well seve as a "laundry list", or point of departure, for the courts or the Tribunal in determining whether competition has been lessened substantially. Alternatively, if the post-merger increase in concentration does not increase the HHI by 100 points, the DOJ is unlikely to challenge. The 1984 Guidelines remark on a conceivable set of mergering firms that would produce increases in the HHI of 100 points:

> Mergers producing increases in concentration close to the 100 point threshold include those between firms with market shares of 25 percent and 2 percent, 16 percent and 3 percent, 12 percent and 4 percent, 10 percent and 5 percent, 8 percent and 6 percent, and 7

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[12] *Supra*, n. 1, at par. 4493.101, s. 3.11.

[13] The 1982 Guidelines stated that the DOJ was "more likely than not "to challenge a merger in a moderately concentrated market if the HHI was greater than 100 points. See: 1982 Guidelines, at para. 4503.101, section III A(1).

percent and 7 percent.[14]

Market Highly Concentrated:

In a market in which the shares of the four largest firms amount to approximately 75% or more, the Department will ordinarily challenge mergers between firms accounting for, approximately, the following percentages of the market:

Acquiring Firm	Aquired Firm
4%	4% or more
10%	2% or more
15% or more	1% or more

(Percentages not shown in the above table should be interpolated proportionately to the percentages that are shown.)

Market Less Highly Concentrated:

In a market in which the shares of the four largest firms amount to less than approximately 75%, the Department will ordinarily challenge mergers, between firms accounting for, approximately, the following percentages of the market:

Acquiring Firm	Aquired Firm
5%	5% or more
10%	4% or more
15%	3% or more
20%	2% or more

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[14] Supra, n. 1, at par. 4493.101, s. 3.11, note 16. See: Fox, supra, n. 6, for a comprehensive comparison of the 1982 Guidelines and the 1968 Guidelines. The 1982 Guidelines thresholds have been retained in the 1984 revisions. The 1968 Guidelines, supra, n. 1, set a CR4 threshold of 75 percent, above which the market was deemed "highly concentrated" and below which the market was classified as "less highly concentrated". The level of increased concentration to be challenged was as follows:

25% or more	1% or more

See: 1968 Guidelines, supra, n. 1, at par. 4510, par. 5.

In the highly concentrated markets, generally considered to exhibit a HHI above 1800, the DOJ is unlikely to challenge a merger which gives rise to an increase in concentration of less than 50 points. If, however, the post-merger increase in the HHI resides in the 50 to 100 point range, the Department is likely to challenge the merger unless "the merger is not likely substantially to lessen competition".[15] Again, the 1984 Guidelines offer a set of possible market shares for merging firms that would trigger a challenge:

> Mergers producing increases in concentration close to the 50 point threshold include those between firms with market shares of 12 percent and 2 percent, 8 percent and 3 percent, 6 percent and 4 percent, and 5 percent and 5 percent.[16]

The most certain scenario for anticompetitive repercussions for the DOJ occurs when the HHI exceeds 1800 and the change in the HHI surpasses 100 points. Only in extraordinary cases will the DOJ deduce from the qualitative factors that the merger is not likely substantially to lessen competition.

In an effort to summarize and conceptualize the "sliding scale" concept engendered in the foregoing preliminary decision rules, the following table may be useful:

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[15] Supra, n. 12.

[16] Supra, n. 1, at par. 4493.10, s. 3.1, footnote 17.

Preliminary Decision Rules

Δ HHI

Post-Merger Increase in Concentration

HHI Post-Merger Concentration	0	50	100
unconcentrated	No Challenge	No Challenge	No Challenge
1000 moderately concentrated	Challenge Unlikely	Challenge Unlikely	Challenge Likely Unless Rebutted
1800 highly concentrated	Challenge Unlikely	Challenge Likely Unless Rebutted	Challenge Likely
10,000			

The threshold levels invariably provoke heated debate. The 1984 Guidelines circumvent any new criticism by adopting values analogous to the 1968 CR4 levels. As discussed *supra*, the 1000 and 1800 HHI threshold correspond approximately to

CR4 values of 50 and 70 percent respectively. The precise values of the thresholds notwithstanding, the DOJ expresses an intent to place less emphasis on the specific numbers in any event.

(b) Limitations

Numerous authors have commented on the latent shortcomings of the structural concentration test employed in the 1984 Guidelines.[17] The DOJ expressly acknowledges several pitfalls. First, the guidelines reiterate the imprecision of the numerical thresholds:

> Although the resulting regions provide a useful format for merger analysis, the numerical divisions suggest greater precision than is possible with the available economic tools and information. Other things being equal, cases falling just above and just below a threshold present comparable competitive concerns.[18]

Second, the standards are based on unavailable post-merger data:

> Moreover, because concentrations and market share data present a historical picture of the market, the Department must interpret such data in light of the relevant circumstances and the forward-looking objective of the Guidelines--to determine likely future effects of a given merger.[19]

Bronsteen,[20] in a consolidated review of the revised guidelines, discerns the practical difficulty in estimating the post-merger level of the HHI. As a close approximation, Bronsteen recommends that a range of pre-merger HHI values be estimated and the increase in concentration be added.[31] In addition, the author observes that the aggregation problem arising from affiliated firms has not been addressed.[32] Furthermore, he remarks on the debate surrounding the use of dollar values or unit sales:

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[17] See: the discussion, supr, Chapter VIII F, on the HHI for specific criticisms of the HHI test.

[18] Supra, n. 1, at par. 4493.10, s. 3.1, footnote 17.

[19] Ibid.

[20] Peter Bronsteen, "A Review of the Revised Merger Guidelines", (1984) 29 Antitrust Bulletin 613.

> When output is deemed appropriate for measuring market share, either dollar sales or units sales may be used. ... [I]f the broad product market is indeed justified, then the choice between units or revenues will hinge on judgments regarding the measure that appears most closely related to the possible competitive strength of firms in the market. The proper decision is rarely obvious.[33]

Finally, the "extraordinary case" proviso allows the Department to challenge a merger ostensibly within the safe harbour below 1000 points and to acquiesce to transactions exceeding 1800. Bronsteen speculates that a firm could conceivably possess substantial market power in an unconcentrated market if it held patents on future production or controlled uncommitted capacity.

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[31] Ibid., at p. 644. For example, if the four largest firms consist of market share percentages 20, 15, 10, 5 then, the minimum value for HHI is 750 (assuming all other firms atomistic) and the maximum value is 1000 (assuming 10 other firms at 5 percent). If the third and fourth firm merger, the ?HHI is 100. Consequently, the post merger HHI range is 850 - 1100. As Bronsteen concludes, "[I]t would be prudent to examine the additional factors outlined in the guidelines". (p. 645).

[32] Ibid., at p. 642.

[33] Ibid., at p. 643.

Although the "analytical road mapped out [by the guidelines] is generally sound",[24] Areeda postulates a dynamic problem. The fact that the guidelines do not deal with mergers on the same basis, if they are replicated, may create an incentive to merge early.[25] Unfortunately, this criticism may be leveled at any concentration measurement. Kauper, a former assistant attorney general, describes the DOJ concentration test as guidelines at the upper and lower end "with an essay in the middle".[26] He expresses concern that the guidelines may invite extensive government intervention at the expense of avoiding judicial precedent. Calkins criticizes the measurement of concentration through the use of the HHI and underscores the potential for error in the estimated value of the HHI due to relatively small errors in the market shares of the larger constituent firms.[27] An extremely interesting viewpoint on the determination of the significant market characteristics which predispose the industry to supra competitive pricing is raised by Davidson. The primary prerequisite for market power, he asserts, is the heterogencity of the product. As the products become less differentiated and more homogeneous, the need for antitrust regulation diminishes:

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[24] P. Areeda, "Justice's Merger Guidelines: The General Theory", (1983) 71 Cal. L. Rev. 303, at p. 310.

[25] Ibid.

[26] T. Kauper, "The 1982 Department of Justice Merger Guidelines: An Economic Assessment", (1983) 71 Cal. L. Rev. 497, at p. 513.

[27] Stephen Calkins, "The New Merger Guidelines and the Herfindahl-Hirschman Index", (1983) 71 Cal. L. Rev. 402.

> Both product homogeneity and market segmentation can facilitate the development of market power. Thus, both ought to be included as "Other Factors" that may indicate when concentration indices understate market power. For different reasons, both can facilitate explicit price agreements or their equivalent--homogeneity because it reduces the terms that must be agreed to and monitored, and segmentation because it reduces the incentive to cheat.[28]

It is submitted that, althought the HHI test does not directly handle the issue of product homogeneity, the delineation of the market in section 2 and the nature of the product in section 3.4 do incoporate Davidson's suggestion.

Although the DOJ's structural concentration test raises concerns which cannot be discarded satisfactorily, it does provide a clear and dependable starting point for the analysis of mergers and their resulting impact on social welfare. As Fox concludes, in an article of great breadth and assistance,

> [W]hile guidelines can be devised to identify mergers not likely to misallocate resources, no guidelines (based on a few objective criteria, such as concentration and market share), can be devised to identify mergers likely to misallocate resources. Those who believe that allocative efficiency is the only appropriate basis for merger policy can take one of two paths if called upon to issue guidelines. They can issue guidelines indicating areas of probably safety and stating a methodology for analyzing those mergers

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[28] K. W. Davidson, "The Competitive Significance of Segmented Markets", (1983) 71 Cal. L. Rev. 445.

> that cannot be screened out by simple objective criteria. Or, they can compromise economic principles and provide guidelines even for concentrated markets, perhaps hoping to move antitrust toward a less interventionist regime.[30]

As Coxon and Jones in a recent Canadian study conclude:

> We are not arguing the extreme view-that concentration should be the key enforcement variable, for example-but suggest that in cases where prevention is better than cure (for instance with mergers) structural criteria can be apropos.[31]

3. Qualitative Factors

(a) Introduction

The 1984 Guidelines acknowledge that the concentration test set forth in section 3.1 is not conclusive of market behaviour and performance. Four further characteristics are made available to assist in the evaluation of the "grey areas"; These intermediate areas consist of moderately concentrated markets in which a merger increases the HHI by at least 100 points and highly concentrated markets sustaining a merger which enlarges the HHI by more than 50 but less than 100 points. In broad terms, the four "tilt" factors, which are to be discussed below, include:

(1) Section 3.2, Forward Looking Factors:[32]

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[30] Fox, supra, n. 6, at p. 296.

[31] P. J. Coxon and J. C. H. Jones, "Positive Economics and Public Policy: Some Canadian Evidence on Policy Change and Antitrust", (1985) 30 Antitrust Bulletin 365.

[32] Sections 3.2 and 3.5 were not included in the 1982 Guidelines.

This section includes several factors which should be considered when interpreting the significance of the market shares, particularly foreign competition.

(2) Section 3.3, Ease of Entry:
The entire spectrum of barriers to entry may be addressed under this rubric.

(3) Section 3.4, Other Factors:
In addition to the "Leading Firm Proviso" infra, the guidelines acknowledge the "collusion" theory of oligopolistic behaviour by including in this section a replete "shopping basket" of variables that could conceivably affect the likelihood of inter-firm collusion.

(4) Section 3.5, Efficiencies.

(b) Forward Looking Factors

The 1984 Guidelines postulate three examples of situations in which the market concentration data may overstate or underestimate the likely future competitive significance of the merger. Although the guidelines are not explicit, it would seem a logical inference that the adjustment would be made to the value of the market share prior to the calculation of the corresponding HHI.

The first example advanced concedes that changing market conditions which effect reasonably predictable outcomes may be relevant in interpreting the relevant significance of market shares. As the guidelines illustrate:

> For example, if a new technology that is important to long-term competitive viability is not available to a particular firm, the Department may conclude that the historical market share of the firm overstates the firm's future competitive significance.[33]

The financial condition of the firm is tendered as the second example of an interpretive factor.

> If the financial difficulties of a firm cannot be explained as phenomena of, for example, the business cycle but clearly reflect an underlying structural weakness of the firm, the firm's current market share may overstate its likely future competitive significance. For example, a firm's current market share may overstate its future competitive significance if that firm has chronic financial difficulties resulting from obsolete productive facilities in a market experiencing a long-term decline in demand.[34]

This mitigating factor must be distinguished from the failing company doctrine.[35] The failing company doctrine is an absolute defence to an otherwise unlawful merger and is construed strictly.

By far the most important special interpretative factor under this head is the prominant role accorded foreign competition in section 3.23 of the 1984 Guidelines. As the Department assures:

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[33] Supra, n. 1, at par. 4493.201, s. 3.21.
[34] Ibid., at par. 4493.202, s. 3.22.
[35] See: 1984 Guidelines, at para. 4495, s. 5; See also the discussion infra, Chapter IX, E.

> In all cases addressed by this section of the Guidelines (Section 3.23), the Department will make appropriate adjustment in its analysis of the available data to reflect more accurately actual competitive concerns.[36]

Two examples of special factors affecting the competitive position of foreign firms are cited: percentage quotas and exchange rates. The guidelines recognize the negative relation between domestic price changes and imports subject to percentage quotas:

> In the case of restraints that limit imports to some percentage of the total amount of the product sold in the United States (i.e., percentage quotas), a domestic price increase that reduces domestic consumption would actually reduce the volume of imports into the United States. Thus, actual import sales and shipment data will tend to overstate the competitive significance of firms in countries subject to binding quotas.[37]

Additionally, the Department will readjust the market shares depending on the trade restraints imposed by exchange rates:

> Less significant, but still important factors, such as other types of trade restraints and changes in exchange

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[36] Supra, n. 1, at par. 4493.203, s. 2.23.

[37] Ibid.; This concept is a direct application of the principles developed by Abbott and discussed supra. See: A. Abbott, "Foreign Competition and Relevant Market Definition under the Department of Justice's Merger Guidelines", (1985) 30 Antitrust Bulletin 299. Interestingly enough, Coxon and Jones, supra, n. 31, suggest that a decrease in tariff barriors would cause an increase in imports and profits, consequently would be tagged anticompetitive. It is submitted that the countervailing effect of efficiencies has been neglected in this study.

> rates, also may cause actual import sales and shipment data to overstate the future competitive significance of foreign firms.[38]

The underlying problem rests on the uncertainty about the future state of tariffs, quotas and exchange rates. Two possible solutions are available. The conservative approach is to assume that the effect of foreign competition is limited. The alternate view is to make best efforts to predict future occurrences. As Baker and Blumenthal note, the 1984 Guidelines have opted for the latter:

> This choice is politically acceptable. It is not inevitable. Whether it is wise will be seen over time.[39]

Sims and Lande observe that the 1984 Guidelines have progressed somewhat from their predecessor[40] but are uncertain as to the effectiveness of the revisions:

> This is a significant procedural change, but it is difficult to predict its impact. It will focus debate between the parties to a transaction and the division on the subjective significance to be attached to an import restraint rather than a numbers battle, but whether this will mean any difference in outcomes

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[38] Ibid.

[39] D. J. Baker and W. Blumenthal, "The Revised Merger Guidelines: One Step Forward, Two Steps Back", July 9 (1984) The National Law Journal 39.

[40] The 1982 Guidelines asserted that foreign firms "may be subject to additional constraints not present in the purely domestic market". Consequently, the DOJ would be "somewhat more cautious, both in expanding market boundaries beyond the United States and in assessing the likely supply response of specific foreign firms". See: 1982 Guidelines, par. 4502.30, s. III C. The 1984 Guidelines presume that foreign competitors be treated similar to domestic producers.

remains to be seen.[41]

(c) Ease of Entry

In defining the relevant market, all firms that do not presently sell the relevant product using existing facilities but that could easily and economically shift to the product are included in the market. This section 3.3 considers the more substantial and long run competitive effects of new entry either by means of production substitution requiring significant modifications or the construction of new facilities. As the guidelines note:

> "Entry" may occur as firms outside the market enter for the first time or as fringe firms currently in the market greatly expand their current capacity.[42]

The "five-percent test" is again employed to ascertain the ease of entry and probable magnitude in response to a "small but significant and nontransitory" price increase, generally over a two-year time period. "The more difficult entry into the market is, the more likely the Department is to challenge the merger".[43]

The guidelines are vague on what constitutes a barrier to entry. In a comment relegated to a footnote the guidelines enumerate four factors which may hinder entry:

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[41] Joe Sims and Robert Lande, "DOJ adds Revisionist Dollop to '82 Merger Guidelines", June 25 (1984) Legal Times 15.

[42] Supra, n. 1, at footnote 20.

[43] Ibid., par. 4493.30, s. 3.3. See: E. Fox, "The New Merger Guidelines: A Blueprint for Economic Analysis", (1982) 27 Antitrust Bulletin 519, for a description of the "ease of entry" test.

(1) Capital ~~assets~~ are long-lived,
(2) Capital assets are highly specialized,
(3) The market is stagnant, and
(4) A substantial minimum efficient scale of plant is necessary to achieve economies.[44]

It is submitted that the determination of the existence of barriers to entry is at the core of merger antitrust policy. If barriers to entry are high, then the results of the "five-percent test" will indicate that the incumbent firm enjoys a degree of market power. Conversely, if the barriers to entry are low, the hypothetical monopolist will be unable to sustain a supracompetitive price. One is left to infer that the issue of market power is indistinguishable from that of entry barriers.

Baumol, in what may emerge as a very influential paper, develops the concept of the "contestable market". A contestable market is defined as "one into which entry is absolutely free, *and exit is absolutely costless*".[45] As Baumol summarizes, "In short, it is a requirement of contestability that there be no cost discrimination against entrants".[46] It is hypothesized that the welfare properties of contestable markets are derived directly from three attributes of such markets:

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[44] *Ibid*., footnote 21.

[45] W. J. Baumol, "Contestable Markets: An Uprising in the Theory of Industry Structure", (1982) 72 *American Econ. Rev.* 1, at p. 3.

(1) A contestable market never offers more than a normal rate of profit,

(2) They are absent any inefficiency in production at equilibrium, and

(3) No product can be sold at a price below marginal cost.

As Baumol contends:

> Thus we have our third and perhaps most crucial welfare attribute of such perfectly contestable markets-their prices, in equilibrium, must be equal to marginal costs, as is required for Pareto optimality of the "first best" variety. This, along with the conclusion that such markets permit no economic profits and no inefficiency in long-run equilibrium, constitutes their critical properties from the viewpoint of economic welfare.[47]

The concept of the "contestable market" is an imaginery benchmark to which actual market structures cna be compared. The quest of antitrust policy is to develop a means of comparing the actual market structure to the hypothetical optimal social welfare model.

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[46] Ibid., at p. 4. Note: The relationship between contestability and perfect competition is described by Baumol at page 4:

> Their [contestable market] firms need not be small or numerous or independent in their decision making or produce homogeneous products. In short, a perfectly competitive market is necessarily perfectly contestable, but not vice versa.

[47] Ibid.

The first step in developing a rational standard for evaluating the anticompetitive impact of barriers to entry is to define the cause itself. Bain defines the conditions of entry as "the extent to which, in the long run, established firms can elevate their selling prices above the minimum average costs of production and distribution ... without inducing potential entrants to enter the industry".[48] Ferguson defines barriers as "factors that make entry unprofitable while permitting established firms to set price above *marginal* cost, and to persistently earn monopoly return.[49] From the above two definitions, the origin of the "five percent test "adopted in the 1984 Guidelines is not surprising. Stigler steers a middle course by defining barriers "as a cost of producing (at some or every rate of output) which must not be borne by firms already in the industry".[50] As Demsetz points out, these differing definitions permit different opinions about the sources of entry barriers. For example, economies of scale constitute barriers for Bain but not for Stigler. "Advertising and capital requirements create barriers for Bain because they seem correlated with high profit rates, but, so long as these inputs are available on equal terms to all who wish to employ them, they create no barriers for Stigler; while for Ferguson, they create no barriers if they are not a source of scale economies.[51] The difficulty with Bain's and Ferguson's definitions of entry barriers stems from the use of a possible outcome of barriers, high profit rates, to proxy actual barriers. As Demsetz stresses:

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[48] J. S. Bain, *Industrial Organization*, New York: Wiley & Sons, 1968, at p. 252.

[49] J. M. Ferguson, *Advertising and Competitions: Theory, Measurement, Fact*, Cambridge: Ballinger, 1974, at p. 10.

[50] G. J. Stigler, *The Organization of Industry*, Homewood: Richard D. Irwin, 1968, at p. 67.

> Barriers may or may not yield high profit. Even a securely protected monopolist may fail to cover his cost. Barriers that simply are sources of negatively sloped demand curves are easily overlooked by Bain's and Ferguson's definition.[52]

Consequently, it is submitted that the more effecitve approach should adopt Stigler's viewpoint. As alluded to by Posner, "Stigler's definition of a barrier to entry, as a cost that differentially affects new entrants compared to firms already in the market, is now generally accepted".[53] Stated succinctly, the issue is not whether barriers to entry or high concentration levels lead to high profit rates; the policy question should focus on the effect of entry barriers, in Stigler's sense, on competitive behaviour.

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[51] Harold Demsetz, "Barriers to Entry", (1982) 72 American Econ. Rev. 47, at p. 48.

[52] Ibid.

[53] R. Posner, "The Chicago School of Antitrust Analysis", (1979) 127 University of Pennsylvania L. Rev. 925, at p. 945.

The Harvard School argues that barriers to entry do exist and do afford incumbent firms a degree of market power. Turner, in his 1958 article,[54] asserts that tying agreements would construct artificial entry barriers around a market as a result of what Turner entitled the "Leverage Theory". Fundamentally, the leverage hypothesis states if a seller enjoys a monopoly position in one product, the monopoly would realize equivalent market power in the market for the product's indispensable complement. One year later, Kaysen and Turner[55] enumerate an extensive list of entry barriers, including:

(1) economies of scale,
(2) capital requirements,
(3) scarce inputs, and
(4) product differentiation.[56]

Note that no rigorous definition of barriers to entry is offered nor deduced from the assumption that business firms[57] are rational profit maximizers. The authors recommended a "policy of deconcentration". It is interesting that almost two decades later, Areeda and Turner[58] override the previous analysis by proposing "remedial action"[59] only. As a result of the acceptance of Stigler's definition of barriers, economies of scale are dropped from the roster; the remaining three elements, capital requirements, product differentiation and scarce inputs are discounted on the application of reasoning similar in nature to the Chicago school of entry barriers.[60]

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[54] D. F. Turner, "The Validity of Tying Arrangements Under the Antitrust Laws", (1958) 72 Harv. L. Rev. 50, at p. 60-63.

[55] Carl Kaysen and Donald F. Turner, Antitrust Policy: An Economic and Legal Analysis, Chicago: Harvard University Press, 1965.

[56] Ibid., at par. 409.

[57] Ibid.

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[58] Phillip Areeda and D. F. Turner, Antitrust Law, Boston: Little, Brown, 1980.

[59] Ibid., at par. 840.

[60] Even if the Harvard view of entry barriers is accepted, as Ordover and Willig point out, several difficulties persist:

> But most markets are not perfectly contestable, and neither are they protected by insurmountable entry barriers. Thus, the analysis of merger effects must deal with partial or limited entry. The Guidelines contain various suggestions on how to incorproate entry into merger analysis.

See: J. A. Ordover and R. D. Willig, "The 1982 Department of Justice Merger Guidelines: An Economic Assessment", (1983) 71 Cal. L. Rev. 535 at page 563 et seq.. The authors highlight three difficulties: (1) difficulty of prediction, (2) divertibility, (3) overestimation of incumbent's market power.

In contrast, Posner stresses the Chicago outlook:

> Deconcentration policy, then, is critically dependent upon belief in the existence of substantial barriers to entry in many industries. Once "barrier to entry" was redefined as a differentially higher cost borne by the new entrant, the plausibility of supposing that barriers to entry are common, or commonly substantial, diminished sharply. The deconcentrators are thus arguing from an abandoned premise.
>
> See: Supra, n. 51, at p. 946.

In constant and perpetual dynamic conflict with the "traditional" Harvard view of entry availability, the Chicago School expounds its antithetical theory of entry barriers. Relying religiously on basic price theory, with its attendant assumptions of the rational utility maximizing consumer and profit maximizing producer, the "Chicagoites" deduce that the new entrant, in almost all cases, faces an identical cost advantage to that of the incumbent. As Posner elucidates by way of example:

> There was a similar confusion in the concept of a "barrier to entry", a concept that played--and still plays--a large role in thinking about competition. Suppose that it costs $10,000,000 to build the smallest efficient plant to serve some market; then, it was argued, there is a $10,000,000 "barrier to entry", a hurdle a new entrant would have to overcome to serve the market at no disadvantage vis-a-vis esisting firms. But is there really a hurdle? If the $10,000,000 plant has a useful life of, for example, ten years, the annual cost to the new entrant is only $1,000,000. Existing firms bear the same annual cost, assuming that they plan to replace their plants. The new entrant, therefore, is not at any cost disadvantage after all.

> Advertising presents a similar situation. A new entrant, to get his product accepted in the market, may have to launch it with an expensive advertising campaign. Again, this is a capital expenditure, because the effect of the campaign will not be fully used up in the first year. There is no reason to expect the annual cost of this capital expenditure to be any higher than that of firms in the market. They too must spend money on advertising to keep the consumer interested in their products. Most advertising, in fact, depreciates more rapidly than most plants; therefore, it is a lesser "barrier to entry" than having to build a plant (although in the traditional analysis it was considered a greater one). Neither the plant nor the advertising is a

barrier in any useful sense.[61]

This concept of equal discounted present values of the opportunity costs faced by the new entrant and the incumbent is extended to other so called barriers to entry including vertical integration,[62] restricted distribution schemes[63] (RPM), and predation.[64]

Accepting Stigler's definition of barriers, the material search is for costs that have this characteristic. The four examples supra have been discounted; the remaining candidate for a true entry barrier has been proposed by Williamson.[65] As Posner reflects:

> The most sophisticated quester, Oliver Williamson, has found one [barrier]: the uncertainty of the new entrant's prospects may force him to pay a higher risk premium to obtain capital than existing firms must pay. This is a legitimate point. But it is difficult to believe that such a difference in the cost of capital would be enough to prevent entry if the firms in a market were charging prices substantially above their costs. The risk premium is unlikely to be a large franction of the new entrant's costs. Interest and profit are rarely more than ten percent of a manufacturing firm's sales price and often they are a much smaller percentage. Thus, even if a new entrant had to pay a ten percent higher interest rate and (expected) return to shareholders to attract the necessary capital, its total costs would be only about one percent higher than those of the firms already in the market.[66]

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[61] Posner, supra, n. 53, at p. 929-930.
[62] Ibid., at p. 936.
[63] Ibid., at p. 926 and p. 938.
[64] Ibid., at p. 927 and 939.
[65] O. E. Williamson, "Book Review", (1974) 83 Yale L. J. 647.
[66] Ibid., at p. 945.

Posner does not accept this potential encumbrance as a justification for antimerger policy. If one accepts Stigler's definition of entry barriers,[67] one must gravitate inexorably to the irrefutable conclusion that, aside from possibly higher risk premiums, the only effectual barrier to entry is a legal restriction sanctioned by the state. Posner sets the discussion in perspective:

> The Chicago school does not deny that concentration is a factor that facilitates collusion of a sort difficult to detect, although it attaches less significance to concentration per se than do the oligopoly theorists. It asks, rather, how it is that excessive profitability can persist without attracting new entry that will cause prices to fall to the competitive level. ... Persistent concentration implies either that the market in question simply does not have room for many firms (economies of scale) or that some firms are able persistently to obtain abnormal profits by cost reductions or product improvements that competitors and new entrants are unable to duplicate. Neither case is an attractive one for public intervention designed to change the market structure.[67]

As a consequence, if the Chicago view of the world prevails, less weight and concern should be afforded the analytical search for non-legal barriers to entry. Particularly in the light of merger guidelines fashioned for provisional relief, practically no loss in specificity would result from subordinating, even ignoring, the traditionally accepted correlation between barriers to entry and merger induced market power. The global conclusion, to which Posner arrives, corroborates the general premise of this paper that only large mergers in concentrated markets should be the subject of antitrust policy. Furthermore, factors which induce the propensity for collusive conduct[69] should reinforce the "dispersion theory" of market power.

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[67] See: C. Green, Industrial Organization and Policy, (2d) Toronto: McGraw-Hill, 1985, at p. 108.
[68] Ibid., at p. 946-947.

> From these various analyses, a conclusion of great significance for antitrust policy emerges: firms cannot in general obtain or enhance monopoly power by unilateral action unless*, of course, they are irrationally willing to trade profits for position. Conseuqently, the focus of the antitrust laws should not be on unilateral action; if should instead be on: (1) cartels and (2) horizontal mergers large enough either to creat monopoly directly, as in the classic trust cases, or to facilitate cartelization by drastically reducing the number of significant sellers in the market.
>
> > *By this I mean action that does not involve agreement with a competitor. It may, of course, invovle agreement with a customer or supplier, and generally does: even a sale below cost invovles at least an implicit contract between seller and purchaser.[70]

Recently, commentators have endeavored to revive the concept of entry barriers as a relevant parameter in the determination of market power. Doubts are raised about the assumptions buttressing the Chicago view. What if the initiating firm is concerned with sales as well as profits; what if consumers do not price tied-in products as an integrated whole; what if captial markets are not perfect, uncertainty exists, transaction costs and adjustment costs are non-trivial? Domsetz postulates that the "insider-outsider" framework hides the difficult problem of assessing the broader implications for consumer interest of the barrier. "The barrier may reduce the severity of some externality [emphasis added] or it may bring about improved levels of competition in activities other than that of direct concern."[71] Demsetz is arguing that to restrict the concept of barriers to the cost of producing the physical output of an existing firm is too narrow a view. Unfortunately, the author simply formulates the issue; no resolution or policy effective guidelines are offered.

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[69] See: supra., n. 1, 1984 Guidelines, at 4493.40, s. 3.4, "Other Factors".

[70] Posner, supra, n. 53, at p. 928.

> The valuation process must necessarily be one that is rich in intuition and faith, and poor in discernable measurements. A person possessing a deep faith in the strength and beneficient effects of competitive imitation will value the implied tradeoffs differently than a person possessing an equally deep faith in the process of "creative destruction". There exist neither cost-benefit analyses nor market-given prices by which to weigh benefits and costs in most of these tradeoffs. If the concept of barriers to entry is to be policy useful, it must be able to distinguish these cases and attach value weights to them. The entire problem of desirable and undesirable "frictions" in economic systems has resisted analysis when it has not been simply ignored. ... No such analysis exists for the notion of barriers. Our utterances in this regard may be accorded the skepticism appropriate to fairly unadorned opinion.[72]

An innovative circumvention of the entire debate is proposed by Bronsteen. With respect to the 1984 Merger

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[71] Demsetz, supra, n. 51, at p. 48.
[72] Ibid., p. 56-57.

Guidelines, Bronsteen perceives the DOJ focusing on the relevant issue. The guidelines discuss the "ease of entry",[73] not barriers to entry.

> Instead of attempting to resolve the debate over what constitutes a barrier, the guidelines more properly focus on the competitive effect of entry. In a merger analysis it is more important to consider the disciplining effect that entry may or may not have on firms in the industry than it is to argue over the proper characterization of impediments to entry. For example, the time required to build a manufacturing facility may or may not be characterized as a barrier, but it is relevant in determining the impact of entry on the possible exercise of market power.[74]

Although this is a novel twist, it is submitted that it may well be a distinction without a difference. The "ease of entry" will obviously be predicated on the height of the entry barriers.[75] Moreover, this proposition appears to avoid or neglect the general thesis of the Chicago School which preserves only government-sanctioned barriers as viable impediments to outsider infiltration.

(d) Other Factors

From the standpoint of simplicity and predictability, the 1984 Guideliens degenerate at this stage into a "laundry list" of "other factors" which the DOJ will consider. It is submitted that the common thread which binds these seemingly diverse and disparate factors is their propensity to cultivate collusive behaviour.[76] In practice, these "other factors" are recognizing the alternate source of market power, the "collusion theory". However, this less rigorous approach to collusive behaviour is relegated to a subordinate position; in what appears to be a carry-over from the 1982 Guidelines, the Department will resort to these factors only where the decision "to challenge a merger is otherwise close".[77]

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[73] 1984 Guidelines, supra, n. 1, at 4493.30, s. 3.3.

[74] Bronsteen, supra, n. 20, at p. 647.

[75] The examples cited in footnote 21, 1984 Guidelines, do not restrict themselves to "ease of entry" possibilities; rather they address the "traditional" forms of barriers to entry.

In an effort to categorize the enumerated inventory of relevant factors which could likely influence the ease of collusion in the market, the following Table I may be helpful:

Table I[78]

Factors Which May Increase The
Propensity to Collude

1. The product is homogeneous and undifferentiated (s.

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[76] 1984 Guidelines, supra, n. 1, at para. 4493.40, s. 3.4: "[T]he Department will consider the following factors, among others, as they relate to the ease and profitability of collusion".

[77] 1984 Guidelines, supra, n. 1, at 4493.40, s. 3.4. Note: In the 1982 Guidelines, the "other factors" were integrated into the preliminary decision standard under section IIIC. The 1982 Guidelines made use of these factors in two principal cases: first, in a moderately concentrated market where the HHI is greater than 100 and second, in a highly concentrated market where the HHI is greater than 50 but less than 100 points. In the 1984 Guidelines, these limitations are not present.

[78] See: E. M. Fox, "The New Merger Guidelines - A Blueprint for Microeconomic Analysis", (1982) 27 Antitrust Bulletin 520, at pp. 539-541, for a similar table.

3.411);

2. A large "gap" exists at the edge of the product and geographic markets (s. 3.412);
3. The products or plants are particularly good substitutes (s. 3.413);
4. The participating firms can quickly detect and retaliate against cheaters (s. 3.42);
5. Orders are frequent, regular and small (s. 3.42);
6. Fringe firms are not able to respond profitably to a "small but significant and non-transitory" price increase (s. 3.43);
7. The firm has previously engaged in horizontal collusion (s. 3.44(a));
8. The firm is engaged in potentially anticompetitive conduct such as delivered pricing, price protection clauses (s. 3.44(b));
9. The acquired firm is a disruptive firm (s. 3.44(c));
10. The proposed merger would occur in a market currently performing anticompetitively (s. 3.45).

Notice that several of these elements, such as product differentiation and supply substitution, are replications of factors previously included in the HHI analysis of section 3.11. Moreover, these variables do not lend themselves easily to mechanical tests; they are issues of a more qualitative nature which require reasoned and knowledgeable judgement to apply. In the sphere of provisional relief, this battery of collusion-predicting factors is, at best, of tertiary significance.

(e) Efficiencies

The American posture for all practical purposes has been reversed with regard to its stance on the role of efficiencies in merger guidelines. The landmark judgement of the U.S. Supreme Court in Philadelphia National Bank[79] decried the justification of an otherwise anticompetitive merger on efficiency grounds:

> [A] merger the effect of which 'may be substantially to lessen competition' is not saved because, on some ultimate reckoning of social or economic debits and credits, it may be deemed beneficial. A value choice of such magnitude is beyond the ordinary limits of judicial competence, and in any event has been made for us already, by Congress when it enacted the amended [Sec.] 7. Congress determined to preserve our traditionally competitive economy. It therefore proscribed anticompetitive mergers, the benign and the malignant alike, fully aware, we must assume, that some price might have to be paid.[80]

The 1968 Guidelines perpetuated the rejection of the efficiencies defence:

> Unless there are exceptional circumstances, the Department will not accept as a justification for an acquisition normally subject ot challenge under its horizontal merger standards the claim that the merger will produce economies (i.e., improvements in efficiency) because, among other reasons, (i) the Department's adherence to the standards will usually result in no challenge being made to mergers of the kind most likely to invovle companies operating significantly below the size necessary to achieve significant economies of scale; (ii) where substantial economies are potentially available to a firm, they can normally be realized through internal expansion; and (iii) there usually are severe difficulties in accurately establishing the existence and magnitude of economies claimed for a merger.[81]

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[79] U.S. v. Philadelphia National Bank, 374. U.S. 321 (1963).
[80] Ibid., at p. 371.
[81] 1968 Guidelines, supra, n. 1, at para. 10.

The 1982 Guidelines were similarly proscriptive:

> Except in extraordinary cases, the Department will not consider a claim of specific efficiencies as a mitigating factor for a merger that would otherwise be challenged. Plausible efficiencies are far easier to allege than to prove. Moreover, even if the existence of efficiencies were clear, their magnitudes would be extremely difficult to determine.[82]

The Department proclaimed that in any event the defence would only be considered in what were otherwise close cases.[83]

The 1984 Guidelines, recognizing that most mergers do not create a "significant danger to competition", shift efficiency considerations from a defence to a qualitative factor.[84] The Department undertakes:

> As a consequence, in the majority of cases, the Guidelines will allow firms to achieve available efficiencies through mergers without interference from the Department.[85]

In cases where the merger fosters "competitive risks", the Guidelines will balance thees anticompetitive effects against "clear and convincing evidence" of significant expected net efficiencies arising from the merger. Examples of possible efficiencies are noted:

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[82] 1984 Guidelines, *supra*, n. 1, at s. V (A).

[83] *Ibid*., at footnote 55.

[84] 1984 Guidelines, *supra*, n. 1, at 4493.50, s. 35. For reviews of the efficiency defence in the Guidelines, see: Fox, *supra*, n. 78, at p. 547; Pfunder, M.R., "Defenses and Justifications Under the Guidelines", *New Merger Guidelines*, ed. by J. Shenefield, Practising Law Institute, 1982, at p. 57-62; Richard A. Miller, "Notes on the 1984 Merger Guidelines: Clarification of the Policy or Repeal of the Cellar - Kefauver Act", (1984) 29 *Antitrust Bulletin* 653; Baker, at p. 40 *supra*, n. 39; Sims, at p. 18 *supra*, n. 41; Areeda, at p. 172-199, *supra*, n. 58; T. J. Muris, "The Efficiency Defense Under Section 7 of the Clayton Act", (1980) 30 *Case W. Res. L. Rev.* 153.

[85] *Ibid*.

> Cognizable efficiencies include, but are not limited to, achieving economies of scale, better integration of production facilities, plant specialization, lower transportation costs, and similar efficiencies relating to specific manufacturing, servicing, or distribution operations of the merging firms. The Department may also consider claimed efficiencies resulting from reductions in general selling, administrative, and overhead expenses, or that otherwise do not relate to specific manufacturing, servicing, or distribution operations of the merging firms, although, as a practical matter, these types of efficiencies may be difficult to demonstrate.[86]

As well, the DOJ will reject claims of efficiency if equivalent savings can be achieved through alternate means.[87] A tolerance for the efficiency argument has been transmitted by the DOJ which is in sharp contrast to its own views expressed in the original guidelines.

When modifying the American approach to the Canadian injunctive setting, for several reasons a major alteration needs to be accomplished. As a general axiom, guidelines cannot be more restrictive than the substantive law as defined by the governing statute and attendant jurisprudence. In the case of the Competition Act, s. 68(1) sets forth the rudiments of the efficiency defence:

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[86] Ibid.

[87] Note that the DOJ will give more weight to efficiencies when challenging a vertical rather than a horizontal merger. One might suspect greater efficiencies from vertical mergers.

> 68. (1) The Tribunal shall not make an order under section 64 if it finds that the merger or proposed merger in respect of which the application is made has brought about or is likely to bring about gains in efficiency that will be greater than, and will offset, the effects of any prevention or lessening of competition that will result or is likely to result from the merger or proposed merger and that the gains in efficiency would not likely be attained if order were made.[88]

For the guidelines to be less restrictive, a permissable defence must be more restrictive. This could be accomplished in two possible fashions. First, the efficiency defence could be deleted altogether. The difficulty with this desultory approach is the inherent and potentially inexplicable contradiction between its inclusion in the substantive provisions and deletion in the guidelines. The preferable tack is to include the defence in the guidelines but impose a heavy burden of proof on the potential respondent. The 1984 Guidelines may achieve a burden of proof exceeding the usual civil preponderance of evidence test by requiring "clear and convincing evidence". Nonetheless, guidelines groomed for prosecutorial discretion regarding provisional proceedings would be weakened if the efficiency defence envisioned in s. 68 Competition Act were transplanted into guidelines. An indepth review of possible future efficiency gains balanced against potential anticompetitive repercussions is more appropriately postponed to a trial on the merits before the Tribunal.

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[88] Competition Act, S.C. 1986, (formerly Bill C-91), s. 68 (1).

Several reasons partially justify the downplaying of the efficiency defence in merger guidelines. First, the probability of market power in the foreseeable future should not be neutralized be short-run expected economies of scale. Secondly, as mentioned above, it is impossible from a practical viewpoint to predict whether economies of scale will be realized, their magnitude and duration. Thirdly, if the concentration bright lines are set relatively high, any conceivable efficiencies are likely to be overwhelmed by market power. At such high threshold levels, it is unlikely that a merger which increases concentration substantially is the only route to attain the efficiencies. Indeed, at these high levels of concentration managerial economies are the most likely form of efficiency, and these are extremely problematic. In short, by implementing appropriately high threshold values, the efficiency defence may be relegated to a subordinate priority. As Professor Sullivan warned in his statement before the Subcommittee on Monopolies and Commercial Law, U.S. House of Representatives, 7 March, 1985:

> Whether or not a particular merger will lead to a better use of existing resources is almost always an open question, one that even well informed and

experienced people can only guess about.[89]

In sum, it is recommended that the availability of the efficiency defence be acknowledged in injunctive guidelines; however the burden of proof resting with the respondent should be expressly and unequivocably imposed in the range of high or strong probabilities.

4. THE 1984 REVISIONS TO THE 1982 GUIDELINES

In order to discern the trend in American antitrust policy, an overview of the amendments to the 1982 Guidelines is helpful. The 1982 Guidelines exhibited a quantum leap in conceptual underpinnings from the godfather of guidelines developed in 1968. In contrast, the 1984 Guideliens retained the principal constructs of their predecessor and imposed only minor fine-tuning adjustments. It is for this reason that references to the fundamental tests contained in the 1982 Guidelines are for the most part sufficient when discussing the 1984 version. Notwithstanding this general adaption, the 1984 Guidelines recommend three substantial changes in policy orientation and several minor amendments.

The three major "improvements" contained in the 1984 Guidelines are:

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[89] L. A. Sullivan, "The Justice Department Guidelines on Mergers and Vertical Restraints: A Critique", (1984) 16 Antitrust Law and Economic Review 11.

(1) Supply substitition:

The time period within which the "five percent test" will be applied for the determination of supply substitutability has been extended from six months to one year. This change ensures that the test for supply substitution conforms with its counterpart for demand substitution.

(2) Efficiencies:

As discussed supra, the efficiency defence has been elevated from a defence which was strictly construed to a qualitative factor to be considered by the DOJ.

(3) Foreign Competition:

The same analytical approach will now be applied to foreign as well as domestic competitors.

In addition, minor changes[9] and refinements to market delineation, statistical criteria and other factors support the general observation that the 1984 Guidelines are becoming more permissive and tolerant of most mergers. It also appears that there is widespread acceptance of the economic literature investigating merger activity, particularly the body of research affiliated with Landes and

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[9] See Appendix H for a list of changes to the 1982 Guidelines. See also: Neal R. Stoll, "2nd Anniversary Edition of the Merger Guidelines", July 17 (1984) 192 New York L. J. 1; R. A. Miller, "Notes on the 1984 Merger Guidelines: Clarification of the Policy or Repeal of the Cellar - Kefauver Act?", (1984) 29 Antitrust Bulletin 653.

Posner's leading article. Unfortunately, in the American development of merger guidelines, the DOJ may be approaching the status of a de facto regulator, a caution which the Canadian counterparts may be well advised to heed.

5. THE LEADING FIRM PROVISO

The leading firm proviso strives to address the concept of the dominant firm and its ability to act as the price leader in the industry. In principle the doctrine is quite straightforward; a relatively large firm has the capability to set a supracompetitive price and then "coerce" the other members of the industry to follow its lead.

Several important characteristics are implied in the notion of the dominant firm. First, the leading firm must be relatively large; several equally large producers operating in an oligopolistic setting will not supply the requisite environment for a dominant firm to emerge, although the possibility is not excluded. Secondly, any possible merger in an industry in which a dominant firm prevails should be reviewable if it enhances the leading firm's position. Stated alternately, a merger between two of the fringe competitors should be welcome. Third, any acquisition in the market which is de minimum in the sense that the acquired firm's market share is extremely insignificant should merely be ignored. And lastly, the doctrine presupposes that collusive behaviour is almost a certainty due to the dominant position of the leading firm. In this respect, the leading firm proviso is an extension of the "dispersion theory" which correlates anticompetitive performance to increased dispersion amongst the members of the market.

The 1968 Guidelines were mute on the issue of the leading firm phenomenon. The 1982 version of the Guidelines, the Department voiced its concern that a merger between a large and a small member of the market might pass scrutiny under the general standards of the test. For example, a merger between a leading firm with 20 percent of the market and a fringe firm enjoying 2 percent of the market would be bypassed in a moderately concentrated market. In order to preserve the right to prohibit such mergers, the Department stated in section III A (2) that it was:

> likely to challenge the merger of any firm with a market share of at least 1 percent with the leading firm in the market, provided that the leading firm has a market share that is at least 35 percent and is approximately twice as large as that of the second largest firm in the market.

The Department preempts the discussion of factors which may facilitate collusion found in section III C because the ease of collusion is deemed to be of little relevance to the ability of a single dominant firm to exercise market power. Small mergers are exempt and economies are for all intents and purposes ignored.

The 1982 provisions strive to guarantee that the dominant firm is relatively large by requiring that it be twice as large as the next largest incumbent. In addition the thresholds for market shares attempt to guarantee that the acquisition to be questioned involves the purchase by a large firm of a small but not insignificant competitor. In the 1982 Guidelines, the qualitative elements of "forward looking factors" and "efficiencies" were not included in the modification process applied to the strict structural test. If barriers to entry were found to be high, then the ability of the dominant firm to "lead" the industry would also be proportionately high; if the entry barriers were low, the dominant firm would be more likely to consider the potential for competition. This dominant behaviour would be independent of other factors enumerated in sectino III C which might induce collusion.

The 1984 Guidelines unexplainably delete the condition that the dominant firm be at least twice as large as the second largest competitor. It is submitted that this omission could raise difficulties in defining a relatively large leading firm. In addition, the latest version of the Guidelines indicate that they will consider "forward looking factors" and "economies" when evaluating an otherwise leading firm scenario. Although acceptable in theory, this approach opens the floodgates to protracted defence arguments which may be less than fruitful, particularly in the light of the fact that the achievement of economies in such lopsided acquisitions would be extremely unlikely.

In applying the American leading firm provisio to the development of Canadian injunctive guidelines, it would be advisable to retain some mechanism to establish that the leading firm is relatively larger than the other members of hte market. In addition, the qualitative factors, with possibly the exception of entry barriers, should be obviated entirely. On a more general level, it is not at all clear whether the leading firm proviso has any role to play given the Canadian economic environment. As discussed earlier, the change in the HHI thresholds should probably be increased from the American cut-off levels of 50 and 100 point; nonetheless, either the acquiring or acquired firm would have to be relatively small in comparison to the total market in order that the merger could avoid triggering detection by the general test. As a policy recommendation, the potential complications concomittant with the inclusion of the leading firm proviso in injunctive guidelines would outweight the beneficient effects of identifying unusual and extraordinary Canadian cases.

6. CONCLUSIONS

Calvin Goldman, the recently appointed Director under the fledging Canadian Competition Act, in an address to the Canadian Bar Association in Edmonton on 18 August, 1986, assured the audience that a comprehensive programme of compliance would be given top priority under his administration. As well as promoting undertakings and consent/prohibition orders, the dissemination of information to the public completes the tripartite package of policy tools available to the Director for achieving his objective of compliance. Goldman expressed the view that this educational objective could be accomplished by the following means:

(1) The encouragement of consultation,

(2) Speaking engagements by the members of the Bureau of Competition Policy, and

(3) The promulgation of pamphlets, newsletters, annual reports, interpretation bulletins and, most interestingly, enforcement guidelines.

This officially sanctioned encouragement should supply the impetus for the formulation of indigenous Canadian merger guidelines governing the administrative decision-making procedure for pre-trial injunctive relief.

It is recommended that the acceptability of a propsed merger employ (at the core of the test) one of the numerous summary concentration measures. Because of its relative simplicity and well recognized applicability, the HHI is certainly a logical first choice. In addition, the HHI may amalgamate the frequently antipodal theories of dispersion and collusion into one integrated yardstick of market power.[91] Moreover, the HHI may be estimated from the available data on the market shares of large members of the industry. In the Canadian context, it may be advisable to simply delete the American "moderately concentrated" market designation and partition the set of possible markets into two subsets, safe harbours and highly concentrated markets.[92] The absolute level of the HHI threshold and the change in the index resulting from the merger should be defined after empirical economic study solely; avoidance of "politicizing" this process is advised.[93] As an overriding principle, it is recommended that the Canadian thresholds be higher than their American counterparts in order to ensure that the "net" will catch only sizeable transactions in highly concentrated dominant sectors of the economy.

As has been stressed repeatedly throughout this paper, the fulcrum, upon which the entire analysis of potentially anticompetitive effects teeters, is the delineation of the relevant market. Guidelines which methodically develop the concepts of supply and geographic substitutability, as well as demand interchangeability, would be invaluable as a signal to the business and legal communities not to neglect these relevant issues. Other relevant factors, including the existence of price discrimination, product differentiation, or the extent of foreign competition, should be explicitly integrated and clearly understood to play a prominant role in the process. As Donald Baker has articulated respecting the 1984 American approach:

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[91] Since the HHI is directly related to the sum of the squares of market share deviations about their mean the dispersion theory is included; because the HHI is inversely related to the number of members in the industry, one arm of the collusion hypothesis is incorporated.

[92] This designation is similar to the 1982 Guidelines.

[93] The ambiguous results of the 1981 Proposals for Reform stand as testimony to the impossibility of reaching consensus by employing the politically fashionable technique of "consultation".

> The guidelines rightly recognize that no enforcement formulas using statistics can be any better than the markets within which the statistics are calculated. The extensive discussion of market definition-which is at the heart of almost every contested merger case-may over time help focus the department's (and hopefully the FTC's) case selection in the short run, and in the long run may help drive the courts toward substantive legal standards which are both economically rational and administrable in recurring cases.[14]

Subsequent to a determination of the relevant market and the application of the preliminary structural test for market power (HHI), the American procedure turns to a rather detailed examination of other "qualitative factors" which may relate to the profitability of collusion, the ease of entry and the possibility of counterbalancing efficiencies. The retention and enhancement of these other factors in the 1984 Guidelines has forced Neal Stoll to observe:

> If anything, the Guidelines make clear that in hard cases there are few numerical solutions and that a variety of relevant subjective factors will be considered in the determination of a proposed merger's

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[14] Baker, supra, n. 5, at p. 24.

> competitive impact. Ultimately, then, the "Second Anniversary Edition" of the Guidelines provides proponents of potential mergers with an even greater opportunity to make creative arguments in support of their positions.[93]

Because the HHI does measure to some extent the ease of collusion, the existence of entry barriers nebulous and the measurement of efficiencies protracted, it is wise counsel that these other qualitative factors fulfill only an adjuvant role in the formulation of injunctive guidelines.

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[93] Stoll, supra., n. 88, at p. 2.

D VERTICAL AND CONGLOMERATE MERGERS

1. INTRODUCTION

The new Competition Act asserts as its primary objective the encouragement of competition in order to provide consumers with competitive prices and product choices.[1] Consequently, the principal focus of the Act is directed towards anticompetitive effects resulting from horizontal mergers. More recently, however, concern has been raised regarding the effects of "diversified mergers". The following discussion attempts to discover whether preliminary injunction guidelines should incorporate references to these siblings of the traditional horizontal merger and in what direction the substantive standards should move.

Horizontal mergers are defined as acquisitions involving firms either buying or selling close substitutes in the same market. By definition, these forms of mergers inherently alter the competitive structure of the relevant market while possessing the potential for future efficiency gains. Non-horizontal, or diversified, mergers are categorized into two distinct subgroups. Vertical mergers are characterized by the acquisition by a firm of either its supplier or its customer, a transaction along the same production chain. Conglomerate mergers are a residual category of acquisitions involving a company neither in competition with nor in a supplier-customer relation with the acquired firm. In the American jurisprudence, conglomerate mergers are further divided into three subcategories:

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[1] Competition Act, S.C. 1986, Royal Assent 16 June 1986; proclaimed 19 June, 1986, s. 1.1.

(1) Product extension merger:
The producer of one product acquires the producer of a related product in the same market,

(2) Geographic or market extension merger:
The producer in one market acquires the producer of a close substitute in a contiguous market, and

(3) "Pure" conglomerate merger:
The acquiring firm acquires the producer of an unrelated product in a separate market.

The fundamental question plaquing antitrust theorists is how to monitor the desirability of such mergers. The perplexing issue may be reduced to a manageable form when one realizes that both vertical and conglomerate mergers may induce horizontal anticompetitive effects. Vertical mergers may foster foreclosure of markets and may facilitate collusion. Product or geographic conglomerate mergers may stultify potential competition and rate regulation. Unfortunately, the analysis of "pure" conglomerate mergers, their effect on economic performance and their potential for realizing economic efficiencies remains at the stage of paradoxical opinion.

In many instances, the impact of non-horizontal merger acquisitions is manifest, not on concentration *per se*, nor even on the intermediate target of competitive behaviour, but rather the intensification of aggregate concentration.[2] As a percentage of total mergers, non-horizontal mergers have increased their share from thirty-two percent in 1961 to sixty-one percent in 1979.[3] Particular attention has been directed towards the costs and beneifts associated with these types of mergers.[4] The following analysis considers the suitability of including non-horizontal and "pure" conglomerate mergers for Canadian administrative guidelines.

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[2] For a discussion of aggregate concentration, see: F. M. Scherer, *Industrial Market Structure and Economic Performance*, Chicago: Rand McNally, 1980, at p. 64; C. Green, "Industrial Organization and Policy", (2d) Toronto: McGraw Hill, 1985, at p. 75; Canada. "Report of the Royal Commission on Corporate Concentration", Ottawa: Supply & Services Canada, 1980, at pp. 13-31, 103-131, 140-148.

[3] J. Baldwin and P. Gorecki, "Mergers and Merger Policy in the Canadian Manufacturing Sector: 1971-79", Discussion Paper No. 297, Ottawa: Economic Council of Canada, 1986; See: "Mergers can boost competition", (1986) 7 *Au Courant* 13, at p. 13 for a summary of the preceding article.

[4] See: P. Areeda and D. Turner, *Antitrust Law*, Toronto: Little, Brown & Co., 1980, at par. 1100-1152; Bryan. "Conglomerate Mergers: Proposed Guidelines", (1973) 11 *Harv. J. on Legis.* 31; Davidow, "Conglomerate Concentration and Section Seven: The Limitations of the Antimerger Act", (1968) 68 *Colum. L. Rev.* 1231; Mantell. "Conglomerate Mergers, Allocative Efficiency, Allocative Efficiency, and Section 7 of the Clayton Act", (1978) 56 *Tax. L. Rev.* 207; R. Posner, *Antitrust Law*, Chicago: University of Chicago Press, 1976; at p. 113.

As a general proposition, and one that has not been succintly summarized in the antiturst literature, the general standard against which to judge diversified mergers should guage the resultant diminution of potential entry. It is obvious that a diversified merger which obviates a potential entrant, either perceived or actual, would satisfy this test. However, it is submitted that an increase in the height of possible barriers to entry does in actual fact accomplish the identical result by diminishing the potential for new entry. In the same vein, the ability of the members of the industry to collude is predicated on the implied assumption that entry impediments are sufficient to permit such conduct. In short, the issues of potential entry, barriers to entry, and collusive conduct are merely congruent Hypothesis, different perceptual spokes radiating from the identical theoretical hub.

As an illustration of this synonymity, it may be instructive to illustrate the interrelation between the concept of barriers to entry outlined by Green[5] and the doctrines of potential competition and collusion. Green suggests that one line of reasoning proposes that "limit pricing"[6] may be employed by incumbent firms to deter entry:

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[5] Green, supra, n. 2, at p. 110-118.
[6] See: Scherer, supra, n. 2, at p. 232-252.

> For example, suppose that because of its access to a cheap source of some scarce but essential raw material input, or to patent-protected know how, the established firm's unit costs of production is 10.1 percent lower than the lowest costs of production that could be achieved by any newcomer (entrant) to the industry. The established firm can thereby deter entry to the industry by limiting its markup of price over unit cost to 10 percent--or less. In other words, the "limit price" is 110 percent of established firm average cost, because that is the highest price the established firm, or firms, can set and still foreclose an entering firm from being profitable.[7]

Alternatively, there have been recent suggestions[8] that a more credible entry-deterring threat is an increase in output accompanied by price cutting in the face of attempted entry:

> Such a strategy requires that the established firm(s), when setting price above cost, hold in reserve excess capacity which would be brought into use should new firms attempt to enter the industry. While holding excess capacity costly, the strategy may be more profitable than a limit price strategy if (a) it allows the established firms to set pre-entry prices higher than the limit price and (b) it is a more credible threat from the viewpoint of potential entrants.[9]

There are two reasons why holding excess capacity is likely to be a more effective entry-deterring strategy than a simple limit-pricing strategy. First, the excess capacity tactic reduces the residual demand curve thus decreasing the possibility for a new entrant to find a profit maximizing output. Second, the output increasing threat is more credible because the incumbent firms have actually committed themselves by financing this excess capacity. In either case, this entry-deterring behaviour by the incumbent firms is concordant with the abatement of potential entrants and the concerted conduct of the member firms. In synoptic form, the creation of barriers to entry permits collusive behaviour and results in the reduction of potential competitors. Recognizing this similarity and the ability of diversified mergers to create entry barriers, the test for diversified mergers may actually be incorporated in the substantive section 64(1) of the Competition Act, by reason of the phraseology "is likely to prevent or lessen, competitor substantially". Consequently, Canadian merger guidelines which neglect to include criteria for evaluating non-horizontal mergers may omit a substantial proportional of increasingly worrisome mergers[10] which may in fact be proscribed by the Act.

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[7] Supra, n. 5, at p. 110.

[8] M. Spence, "Entry, Capacity, Investment and Oligopolistic Pricing", (1977) Bell Journal of Economics 534.

[9] Green, supra, n. 5, at p. 112.

2. AMERICAN APPROACH TO DIVERSIFIED MERGERS PRIOR TO THE 1968 GUIDELINES

Vertical mergers in the United States have traditionally been viewed as possessing the ability to potentially foreclose a market. Possible efficiencies emerging from such mergers were frequently relegated to a subordinate position when balanced against the decrease in competition resulting when a supplier (or customer), in competition with the acquiring firm, was precluded from dealing unincumbered with any customer (or supplier). The argument has been advanced that this form of foreclosure might compel competitors of the acquiring to integrate also, this otherwise unplanned integration effectively constructing an entry barrier to the expansion of existing firms and the entrance of new enterprises.

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[10] This conclusion emerges from the traditional view of barriers to entry. If one accepts the Chicago School orientation, then diversified mergers, like horizontal mergers, pose little threat to economic performance. It is unlikely that the Canadian Bureau of Competition Policy would be able to 'market' the Chicago viewpoint in the present political arena.

Although something of an oddity, the first vertical situation to reach the Supreme Court was the du Pont-General Motors[11] case. The substantive question before the Court queried whether du Pont's acquisition of twenty-three percent of General Motors would effectively foreclose other suppliers from dealing with the automotive corporation. Du Pont argued that its strong position relative to General Motors was based solely on the competitive excellence of its products. However, the Court took note of the increased proportion of General Motors' purchases acquired in subsequent years by du Pont's competitors. The Supreme Court concluded:

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[11] U.S. v. E.I. du Pont de Nemours & Co. 353 U.S. 586 (1957).

> The statutory policy of fostering free competition is obviously furthered when no supplier has an advantage over his competitors from an acquisition of his customer's stock likely to have the effects condemned by the statute . . . . The conclusion upon this record is inescapable that such likelihood was proved as to this acquisition.[12]

The leading judicial pronouncement on American vertical integration jurisprudence is found in the Brown Shoe[13] decision. Chief Justice Warren, in an attempt to arrest the rising tide of economic concentration in the American economy, contended that mergers should be blocked in their incipiency. Although not determinative in the case, the Court viewed the foreclosure of markets to competitors as the fundamental detriment accompanying non-horizontal mergers. Chief Justice Warren's position on the vertical aspect was clear:

> ... the trend towards vertical integration in the shoe industry, when combined with Brown's avowed policy of forcing its own shoes upon its retail subsidiaries, may foreclose competition from a substantial share of the markets ... without producing any countervailiing competitive, economic of social advances.[14]

Even though the Brown-Kinney retail chain enjoyed only a small national market share, the Court argued that the vertical merger would substantially lessen competition:

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[12] Ibid, at p. 607.
[13] Brown Shoe Co., Inc. v. U.S., 370 U.S. 294 (1962).
[14] Ibid., at p. 334.

> The retail outlets of integrated companies, by eliminating wholesalers and by increasing the volume of purchases from the manufacturing division of the enterprise, can market their own brands at prices below those of competing independent retailers. Of course, some of the results of large integrated or chain operations are beneficial to consumers. ... But we cannot fail to recognize Congress' desire to promote competition through the protection of viable, small, locally owned businesses. Congress appreciated that occasional higher costs and prices might result from the maintenance of fragmented industries and markets. It resolved these competing considerations in favor of decentralization. We must give effect to that decision.[15]

The conglomerate merger required the courts to devise new approaches to the analysis of non-horizontal mergers. In the Consolidated Foods[16] case, a major food processor, Consolidated, attempted to acquire Gentry, a supplier; the Supreme Court worried that the merger would enable the combined company to practice reciprocity.[17] Reciprocity, Mr. Justice Douglas indicated, "is one of the congeries of anticompetitive practices at which the antitrust laws are aimed".[18] The leading pre-guidelines decision in Proctor &

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[15] Ibid.

[16] FTC v. Consolidated Foods Corp., 380 U.S. 592 (1965).

[17] Reciprocity characterizes the commercial situation whereby a large buyer is able to coerce its suppliers to purchase from itself, or its affiliates; otherwise the dominant buyer will cancel its orders with these suppliers. The economic effects of reciprocity are uncertain. For pertinent discussion, see: G. W. Stocking and W. F. Meuller, "Business Reciprocity and the Size of Firms", (1957) 30 Journal of Business 73; Joel Dean, "Economic Effects of Reciprocity, Competition, and Mergers", (1963) 8 Antitrust Bulletin 843.

[18] Supra, n. 16, at p. 595.

Gamble[19] wrestled with a product-extension conglomerate merger whereby the acquired firm supplied a complementary product through identical distribution systems in adjoining markets. Mr. Justice Douglas, noting that the law deals with the probability not certainty of lessening competition, added two alternate tests, in addition to the concept of reciprocity, for evaluating the anticompetitive effects of a conglomerate merger. First, the Court proposed the doctrine of entrenchment[20] which described circumstances in which a relatively large firm could "entrench" a smaller target company, making competition by its competitors more difficult. As the Court stated:

> [It] may substantially reduce the competitive structure of the industry by raising entry barriers and by dissuading smaller firms from aggressively competing."[21]

Secondly, Mr. Justice Douglas deduced from the fact that Proctor & Gamble was a prime candidate for entry into the liquid bleach market as a competitor of the acquired firm, Chlorox, that the merger eliminated "the potential competition of the acquiring [emphasis added] firm."[22] In sum, three separate judicial standards had developed prior to the publication of the 1968 Guidelines: reciprocity, entrenchment and potential competition.

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[19] FTC v. Proctor & Gamble Co., 386 U.S. 568 (1967).

[20] The doctrine of entrenchment is substantiated on grounds which, in essence, are identical to the theory of entry barriers i.e. economies of scale, "deep-pockets", predation.

[21] Supra, n. 19, at p. 578.

[22] Ibid.; The potential competition theory was first raised implicitly in two early cases: U.S. v. El Paso Natural Gas Co., 376 U.S. 651 (1964); U.S. v. Penn-Olin, 389 U.S. 308 (1968).

3. THE 1968 GUIDELINES

The DOJ, riding a wave of success through the sixties, promulgated its enforcement intentions in the 1968 Merger Guidelines. The Guidelines, developed during a time of excessive merger activity, were restrictive; conceivably the DOJ expected the Guidelines to both deter merger activity and be adopted by the courts. In practice the Guidelines proved much less effective than the DOJ may have envisioned.

With respect to vertical mergers, the DOJ stressed that its most important enforcement aim could be satisfied by,

> [g]uidelines framed primarily in terms of the market shares of the merging firms and the conditions of entry which already exist in the relevant markets.[33]

Barriers to entry resting on such factors as economies of scale were not questionable; however undesirable barriers to entry, raised by foreclosing equal access to potential customers or suppliers and by facilitating promotional product differentiation, were circumscribed. The DOJ proclaimed that it would ordinarily challenge a merger,

> between a supplying firm, accounting for approximately

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[33] 1968 Merger Guidelines, C.C.H. Trade Reg. Rep. par. 4500, at s. II (11).

> 10% or more of the sales in tis market, and one or more purchasing firms, accounting in toto for approximately 6% or more of the total purchases in the market, unless it clearly appears that there are no significant barriers to entry into the business of the purchasing firm or firms.[24]

Furthermore, where there exists an increased risk of a price or supply squeeze, the DOJ would ordinarily challenge the merger,

> between a supplying firm, accounting for approximately 20% or more of the sales in its market, and a purchasing firm or firms, accounting in toto for approximately 10% or more of the sales in the market in which it sells the product whose manufacture requires the supplying firm's product.[25]

Although the 1968 Guidelines emphasize the "foreclosure doctrine" respecting vertical mergers, the DOJ does not exclude the application of the three approaches outlined in the Proctor & Gamble conglomerate merger case:

(1) Reciprocity:

> "[F]or the purpose of putting competitors of either the acquiring or acquired firm at an unwarranted advantage."

(2) Entrenchment:

> "(i) [T]here has been, or is developing, a significant trend toward vertical integration by merger such that the trend, if unchallenged, would probably raise barriers to entry or impose a competitive disadvantage on unintegrated or partly integrated firms, and (ii) it does not clearly appear that the particular acquisition will result in significant economies of production or distribution

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[24] Ibid., at s. II (12).
[25] Ibid., at s. II (13).

> unrelated to advertising or other promotional economies."

(3) Potential Competition:

> "(b) A less common special situation in which a challenge by the Department can ordinarily be anticipated is the acquisition by a firm of a customer or supplier for the purpose if increasing the difficulty of potential competitors in entering the market of either the acquiring or acquired firm."[16]

Turning to the 1968 Guidelines approach to conglomerate mergers, the Department was primarily concerned with those mergers "involving potential entrants and mergers creating a danger of reciprocal buying ... [or mergers which] threaten to entrench or enhance the market power of the acquired firm."[17]

A structural test was employed to determine when the DOJ would ordinarily challenge a merger between a likely entrant and,

(i) any firm with approximately 25% or more of the market;

(ii) one of the two largest firms in a market in which the shares of the two largest firms amount to approximately 50% or more;

(iii) one of the four largest firms in a market in which the shares of the eight largest firms amount to approximately 75% or more, provided the merging firm's share of the market amounts to approximately 10% or

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[16] All three of these quotes are found in the 1986 Guidelines, supra, n. 23, at s. II (14).

[17] Supra, n. 23, at 4500, s. III (17).

> more, or
>
> (iv) one of the eight largest firms in a market in which the shares of these firms amount to approximately 75% or more, provided either (A) the merging firm's share of the market is not insubstantial and their are no more than one or two likely entrants into the market, or (B) the merging firm is a rapidly growing firm.[28]

Furthermore, elimination of a disruptive competitor was ordinarily challenged. With respect to reciprocal buying, the Department considered a significant danger to be present whenever,

> approximately 15% or more the the total purchases in a market in which one of the merging firms ("the selling firm") sells [*sic*] are accounted for by firms which also make substantial sales in markets where the other merging firm ("the buying firm") is both a substantial buyer and a more substantial buyer than all or most of the competitors of the selling firm.[29]

Lastly, the Department was concerned where the acquisition by a leading firm in a relatively concentrated market served to entrench or increase market power of the smaller acquired firm. The Guidelines cited the following types of mergers as examples:

> (i) a merger which produces a very large disparity in absolute size between the merged firm and the largest remaining firms in the relevant markets;
>
> (ii) a merger of firms producing related products which may induce purchasers, concerned about the merged firm's possible

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[28] *Ibid.*, s. III (18).
[29] *Ibid.*, s. III (19).

> use of leverage, to buy products of the merged firm rather than those of competitors; and
>
> (iii) a merger which may enhance the ability of the merged firm to increase product differentiation in the relevant markets.[38]

In harmony with the general philosophy of the 1968 Guideliens, economies were not available as a justification for an acquisition normally subject to a challenge.

The 1968 Guidelines proved far less effective than the DOJ had initially hoped for several reasons. First, the courts were reluctant to apply the Guidelines and developed their own parallel tests, particularly for potential entry. As discussed supra, Chapter IX B-1 (d) two "potential competition theories" emerged, actual and preceived. The doctrine of "perceived potential competition" was enunciated by the Supreme Court in U.S. vs. Marine Bancorporation, 418 U.S. 602 (1974), at p. 624:

> [The merger is deemed] unlawful [1] if the target market is substantially concentrated, [2] if the acquiring firm has the characteristics, capabilities, and economic incentive to render it a perceived potential de novo entrant, and [3] if the acquiring firm's premerger presence on the fringe of the target market in fact tempered oligopolistic behavior on the part of existing participants in that market.

Later, the Court stated that before a conglomerate merger would be prohibited under the "actual potential competition", the target market had to be substantially concentrated and the potential entrant had to possess,

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[38] Ibid., s. III (20).

> [A]vailable feasible means for entering the [target] market other than by [the challenged acquisition]; and [2] that those means offer a substantial likelihood of ultimately producing deconcentration of that market or other significant procompetitive effects. (at p. 633)

The 1968 Guidelines omit element [3] of perceived and element [2] of actual potential competition and, in addition, raise other hurdles mitigating the effectiveness of these two doctrines.[31] Secondly, the economic rationale was suspect.[32] And thirdly, the economic doctrines and related guidelines were wholly unsuited for application to "pure" conglomerate mergers.

4. THE 1982 AND 1984 MERGER GUIDELINES

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[31] See: J. P. Bauer, "Government Enforcement Policy of Section 7 of the Clayton Act: Carte Blanche for Conglomerate Mergers", (1983) 71 Cal L. R. 348, at p. 358 et seq. See the following cases for judicial notice and often acceptance of the doctrine of perceived potential competition:
U.S. v. Siemens Corp., 621 F. 2d 499 (2nd Cir. 1980);
Yamaha Motor Co. v. FTC, 657, F. 2d 971 (8th Cir., 1981);
Tenneco, Inc. v. FTC, 3 Trade Reg. Rep. (CCH) par. 21, 873 (Sept. 13, 1981);
Mercantile Texas Corp. v. Board of Governors, 538 F. 2d 1255 (5th Cir. 1981);
Republic of Texas v. Board of Governors, 649 F. 2d 1026 (5th Cir. 1981).

The Supreme Court has expressly declined to approve the doctrine of actual potential competition. See: Bancorp., Siemens, supra.

[32] See: R. Bork, The Antitrust Paradox, New York: Basic Books, 1976, at p. 231; R. Posner, Antitrust Law, Chicago: University of Chicago Press, 1976, at p. 159.

Partly due to the widespread appreciation of the perspectives advocated by the Chicago School, the 1982 Guidelines and the 1984 revisions adopted a more permissive approach to non-horizontal mergers. Apart from the promotion of the efficiencies defence, the 1982 and 1984 versions of the Guidelines are for all practical purposes interchangeable. As Attorney General W. F. Smith commented on the trend in the Department's thinking:

> [V]ertical and conglomerate merger cases have ceased to be a major enforcement focus of the [Antitrust] Division.[33]

The Assistant Attorney General, W. Baxter, confirmed this view:

> [M]ergers are rarely, if ever ... troublesome because of their vertical or conglomerate features.[34]

The 1984 Guidelines focus on the horizontal competitive effects of diversified mergers. The Guidelines express that, in the view of the DOJ, non-horizontal mergers are less likely than horizontal mergers to create competitive problems. The approach to vertical mergers abandons the emphasis on significant foreclosure of competitors, central to the 1968 Guidelines, and relies instead on the conditions which might deter entry and facilitate collusion. The Department emphasizes the doctrine of "potential entry" when evaluating conglomerate mergers, discarding for the most part the older standards of reciprocity and entrenchment.[35]

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[33] W. F. Smith, "Comment", (1981) 42 Antitrust and Trade Reg. Rep. (BNA) No. 1025, AA-23.

[34] W. Baxter, "Comment", (1982) 52 Antitrust Law J. 25.

Deferring until latter the issue of vertical mergers accomplishing an evasion of rate regulation, the 1984 Guidelines rely primarily on the analysis of structural characteristics to evaluate the potential for anticompetitive performance which might result from vertical integration. As suggested in the introduction to diversified mergers, the DOJ's bifurcated approach to vertical mergers tends to meld into one essential topic: does the vertical merger enhance the prerequisites for the realization of market power in the "primary market"?[36] The process is subdivided into two perceived competitive problems which might materialize, heightened barriers to entry and increased collusive behaviour.

With respect to the matter of entry barriers, the Department voices concern that a vertical merger may require new entrants to enter at two levels.[37] The Guidelines outline three necessary, but not sufficient, conditions for competitive problems to arise:

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[35] See: Appendix G, for a precise flowchart of the 1984 Guidelines respecting non-horizontal mergers.

[36] "Primary market" refers to the market in which competitive concerns are being considered, and the term "secondary market" refer to the adjacent market.

[37] See: R. Posner, "The Chicago School of Antitrust Analysis", (1979) 127 U. Pa. L. Rev. 925, for a rejection of the economic justification for such concerns.

> First, the degree of vertical integration between the two markets must be so extensive that entrants to one market (the "primary market") also would have to enter the other market (the "secondary market") simultaneously. Second, the requiremenet of entry at the secondary level must make entry at the primary level significantly more difficult and less likely to occur. Finally, the structure and other characteristics of the primary market must be otherwise so conducive to non-competitive performance that the increased difficulty of entry is likely to affect its performance.[38]

To determine the existence of these three criteria, the DOJ will consider and apply the following standards:

(1) Need for Two-Level Entry:[39]

Is excess capacity of the unintegrated secondary market insufficient to support two minimum-efficient-scale plants in the primary market?

(2) Increased Difficulty of Two-Level Entry:[40]

Yet again, the "five percent" test is pulled into service, questioning whether entry into the secondary market is difficult? The Guidelines highlight that differences in capital costs and scale economies between the primary and secondary markets may heighten the entry barriers to two-level entry.

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[38] 1984 Merger Guidelines, CCH Trade Reg. Rep., par. 4494.201, s. 4.21.

[39] Ibid., s. 4.211.

[40] Ibid., s. 4.212.

(3) Structure and Performance of the Primary Market:[41]

Is the value of the HHI in the primary market greater than 1800?

If the response to the preceding three queries is affirmative, then the DOJ is more likely to challenge the merger. In review, it is evident that the Guidelines are intended to address the possibility vertical integration restricting potental entry into a relatively concentrated primary market.

Turning to the second potential concern arising from vertical mergers, the 1984 Guidelines select two specific instances in which vertical integration might facilitate collusion in the upstream market. Both scenarios require the upstream market to be generally conducive to collusion. As a practical standard, the DOJ is unlikely to challenge a vertical merger unless the HHI in the upstream market exceeds 1800.

The underlying economic policy justifying this standard appears to adopt the transaction cost analysis espoused by Oliver Williamson. As Williams concludes:

> Thus, anticompetitive effects are likely to exist in highly concentrated industries; but because vertical

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[41] Ibid., s. 4.213.

integration in low or moderatley concentrated industries is likely to promote efficiency, it will rarely pose an antitrust issue.[42]

In addition to the general requirement that the upstream market be conducive to collusion, the first case would require a large percentage of the products produced in the upstream market to be sold through vertically integrated retail outlets.[43] The Department argues that because retail prices are more visible than prices in upstream markets, collusion is facilitated by making price monitoring easier. Alternatively, the second specialized situation would require the elimination of a disruptive downstream buyer who is significantly more attractive than the other firms in its market.[44]

It is not apparent why the drafters of the 1984 Guidelines have singled out retail price monitoring and disruptive buyer elimination for special consideration and treatment. Even more perplexing is the need to treat entry barriers and variables which facilitate collusion disjunctively.

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[42] See: O.E. Williamson, Canada, House of Commons, "Minutes of Proceedings and Evidence of the Legislative Committee on Bill C-91", No. 1, April 23, 1986, at p. 615. The merger Guidlines focus on the monopoly subset and reflect the importance of asset specificity. For the Guidelines application of these concepts, see: Ibid., s. 4.221, 4.222.

[43] Ibid., s. 4.221.

[44] Ibid., s. 4.222. The DOJ will determine relative "attractiveness" of the disruptive buyer by comparing its volume of purchases or other characteristics to the other firms in the market.

Conglomerate mergers[45] which effectively remove the acquiring firm from the edge or fringe of the market could harm perceived[46] or actual potential competition. It is disturbing that, although the U.S. courts have not affirmed the actual potential competition doctrine, the DOJ has retained the concept in the Guidelines:

> If it were always profit-maximizing for incumbent firms to set price in such a way that all entry was deterred and if information and coordination were sufficient to implement this strategy, harm to perceived potential competition would be the only competitive problem to address. In practice, however, actual potential competition has independent importance. Firms already in the market may not find it optimal to set price low enough to deter all entry; moreover, those firms may misjudge the entry advantages of a particular firm and, therefore, the price necessary to deter its entry.[47]

Because of the close relationship between the two concepts, the Department will evaluate mergers which raise either type of potential competition.

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[45] Note that the elimination of potential entrants is a concern not restricted to conglomerate mergers; any non-horizontal merger may be scrutinized under this standard.

[46] As the 1984 Guidelines explain at s. 4.111:

> By eliminating a significant present competitive threat that constrains the behavior of the firms already in the market, the merger could result in an immediate deterioration in market performance. The economic theory of limiting pricing suggests that monopolists and groups of colluding firms may find it profitable to restrain their pricing in order to deter new entry that is likely to push prices even lower by additing capacity to the market. If the acquiring firm had unique advantages in entering the market, the firms in the market might to able to set a new and higher price after the threat of entry by the acquiring firm was elimniated by the merger.

[47] Supra, n. 38, at par. 4494.102, s. 4.12.

The Department will consider five principal factors in determining the likelihood and magnitude of possible entry as follows:

(1) Market Concentration[48]
Is the acquired firm's market not conducive to collusion determined by an HHI exeeding 1800?

(2) General Entry Conditions[49]
Is entry easy for firms without an entry advantage as a result of employing the "five percent test"?

(3) Acquiring Firm's Entry Advantage[50]
Is the entry advantage possessed by three or more other firms?[51]

(4) Market Share of Acquired Firm[52]

(5) Efficiencies[54]
Do expected net efficiencies outweigh the

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[48] *Ibid.*, s. 4.131.

[49] *Ibid.*, s. 4.132.

[50] *Ibid.*, s. 4.133.

[51] Where there is particularly strong evidence of actual entry of the acquiring firm, the DOJ may challenge notwithstanding the entry advantage is possessed by three or more firms.

[52] *Ibid*, s. 4.134.

[53] If the market share of the acquired firm exceeds twenty percent, the Department will challenge.

[54] *Ibid.*, s. 4.135.

possible anticompetitive effect?

If the responses to the preceding questions are in the engative, then the DOJ is more likely to challenge the merger.

For both vertical and conglomerate mergers, evasion of rate regulation will be scrutinized for sub rosa attempts by the merged company to inflate costs, suppress market transactions or distort resource allocation.[55] Moreover, efficiency arguments will be favourably received by the Department[56]

5. Conclusions

After reviewing the American guidelines for diversified mergers, can one distill certain principles which may be applicable to the development of Canadian injunctive guidelines and which may form a nucleus for Canadian policy orientation. Almost all commentators on the new Competition Act have, prematurely it is suggested, presumed that the substantive provisions of the Act do not apply to conglomerate mergers, at least of the "pure" conglomerate genre. Exemplifying this outlook was the then Minister of Consumer and Corporate Affairs, the Honourable Michel Cote, the expeditor who guided Bill C-91 through the legislative quagmire. Mr. Cote claimed in response to a question on why conglomerate mergers are not the subject to Canadian competition law:

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[55] Ibid., s. 4.23; See also: Appendix G.
[56] Ibid., s. 4.24; See also: Appendix G.

> So in fact we are going to deal with the concentration, but inside the bill and with a [sic] competition mind-that is how we have to deal with that. If a specific transaction, Mr. Orlikow, between two conglomerates would not enhance competition like the bill suggests it should, then it should be disallowed-not because it is a concentration, but because of the competition I expect of it, nothing else. So that is why I am saying that I want to assure you that by such we are dealing with the concentration, but it is not a bill that has to deal with it; it is a bill that is there for the competition aspect.[87]

The Minister appears to support the coverage by the Act of product and geographic market extension conglomerate mergers, as well as vertical mergers, but evades the issue of pure conglomerate mergers. Even the noted authority on Canadian competition policy, Professor William Stanbury, deduces that the new provisions could not apply to "pure" conglomerate mergers:

> *Conglomerates*: The new provisions cannot be used to deal with conglomerate mergers, only horizontal and vertical ones. While s. 63 appears to include conglomerates within the definition of a merger, as it refers to competitors, suppliers, customers and other persons", the critera in s. 64, namely a suhstantial lessening of competition, makes it clear that conglomerate mergers could not be dealt with under Bill C-91. The reason lies in the definition of a true conglomerate merger. It involves two firms who are not in the same industry or market (i.e., not competitors), *and* who are not vertically related to each other, i.e., one is not the supplier or customer of the other.

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[87] Canada. House of Commons. "Minutes of Proceedings and Evidence of the Legislative Committee on Bill C-91", No. 1, April 23, 1986.

> The provisions can deal with a merger involving two conglomerate firms provided that each of the two potential merger partners have in their group a firm that is horizontally or vertically related to another firm in the other group.[58]

With respect, it is submitted that the substantive provisions of the Act do permit the Tribunal to evaluate "pure" conglomerate mergers as well as non-horizontal mergers accompanied by horizontal effects. Section 63 contemplated mergers which result in the acquisition of control of the business of a "competitor, supplier, customer or other person".[59] (emphasis added) In conjunction with this element, section 64(1) of the Act reads in part:

> 64. (1) Where, on application by the Director, the Tribunal finds that a merger or proposed merger prevents or lessens, or is likely to prevent or lessen, competition substantially
>
> (a) in a trade, industry or profession,
>
> (b) among the sources from which a trade, industry or profession obtains a product,
>
> (c) among the outlets through which a trade, industry or profession disposes of a product, or
>
> (d) otherwise than as described in paragraphs (a) to (c)[60]

Recent commentators have focused on the requirement that the merger lessen competition substantially in a trade, the sources of supply or means of outlet;[61] however, the merger may affect competition in a broader context. The Act, pursuant to s. 64(1)(d), does not restrict the evaluation to horizontal effects in the determined relevant market. The possibility is certainly available to interpret s. 64(1)(d) as granting jurisdiction to the Tribunal and the courts to investigate "pure" conglomerate mergers from the perspective of their adverse effects on potential competition. In this sense, the opinions expressed in section 4.1 of the 1984 Guidelines, if properly extended beyond merely horizontal implications, may be applicable to conglomerate guidelines under the Competition Act.

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[58] W. T. Stanbury, "Changing Canada's Competition Law: Analysis of Bill C-91", Brief submitted to Leg. Comm. (April 1986) (unpublished), at p. 24. See also: Canada. House of Commons. "Minutes of Proceedings and Evidence of the Legislative Committee on Bill C-91". No. 3, April 29, 1986.

[59] Competition Act, S.C. 1986, s. 63.

[60] Ibid., s. 64(1).

The 1984 Guidelines have deleted specific reference to the foreclosure aspects of vertical mergers and the reciprocity and entrenchment presence in conglomerate analysis. It is submitted that emphasis on potential entry, and its impairment, is the proper focus for both vertical and conglomerate mergers; the diverse theories of foreclosure, reciprocity and entrenchment can quite conceivably and effectively be funnelled into one all-encompassing test which would monitor the likelihood of potental competition. Moreover, the separation of potential entry analysis into actual or perceived formats, arising from the historical development of the American common law need not be drawn in the Canadian guidelines. The Canadian courts have presently avoided such fine distinctions; the operative question is basically whether the incumbent's behaviour is redirected as a result of expected competition. In this sense, actual potential competition should play an ancillary role at best.

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[61] Ibid., ss. 64(1)(a)(b)(c).

When formulating preliminary injunction guidelines, as a minimum the Director should not be permitted to abdicate responsibility for accessing the horizontal effects of non-horizontal mergers. One must recollect that any analysis of horizontal effects requires, by definition, a delineation of the relevant market; this extremely complex and crucial endeavour cannot be circumvented even in the case of conglomerate mergers. This realization validates the immediate exigency which must be placed on incorporating market delimitation procedures in the guidelines.

If one accepts the premise that the Canadian guidelines should target as suspicious a merger which effects a significant diminution in the likelihood of potential entry, the pragmatic problem still remains of constructing relatively simple criteria to monitor changes in the degree of possible entry. A framework can be excised from the American experience. The first prong of the test would investigate whether the primary market is conducive to collusion. In the case of preliminary relief guidelines, a structural test employing the HHI would not be inappropriate, although the threshold for Canadian sectors may be set above 1800. The second prong would review qualitative factors which could potentially alter the ease of entry of competitors into the primary market. As a first approximation, the procedures developed for applying the American "five percent test" would be recruited for service. The inescapable similarity between the procedures proposed for diversified mergers and the American approach to horizontal mergers in the 1984 Guidelines cannot be overlooked. Mergers which involve a firm in a highly concentrated market and which substantially curtail potential ingression by an outsider would be subject to antitrust proscriptions.[42] As has been demonstrated earlier in the discussion on horizontal mergers, the factors which might facilitate collusion should play a secondary role in evaluating the correctness of granting provisional relief. To embark on such a discovery would embroil the courts in a process amounting to a trial of the merits. Furthermore, the issues outlined in the 1984 Guidelines[43] regarding collusive propensities may be viewed as merely specific instances subsumed under the broader topic of entry capability. The prima facie determination of the inclination of potential competitors to enter the market in question could be adequately approximated by relying on the "five percent test". Simiarly, the argument exhorting the omission of the efficiencies test[44] in provisional injunction guidelines governing horizontal mergers should be adopted for the non-horizontal merger. A fortiori, seldom would "pure" conglomerate mergers ever foster economic efficiencies. And finally, it is submitted that the complexities of rate regulation, and the evasion of governing legislative objectives, should not be the subject of competition legislation; rather policing the avoidance of rate regulation would be more approriately included in the individual regulatory statutes.

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[42] Note: Section 3.1 of the 1984 Guidelines requires the market to be moderately or highly concentrated. Sections 3.2 to 3.5 inclusive require a review of other qualitative factors, namely: forward looking factors, ease of entry, collusive elements and efficiencies.

[43] Supra, n. 38, at s. 3.4.

As early as the 1968 Merger Guidelines, circumspection has accompanied the theorietical knowledge base supporting the antitrust treatment of conglomerate mergers:

> Generally speaking, the conglomerate merger area involves novel problems that have not yet been subjected to as extensive or sustained analysis as those presented by horizontal and vertical emrgers. It is for this reason that the Department's enforecement policy regarding the foregoing category of conglomerate mergers cannot be set forth with greater specificity. Moreover, the conglomerate merger field as a whole is one in which the Department considers it necessary, to a greater extent than with horizontal and vertical mergers, to carry on a continuous analysis and study of the ways in which mergers may have significant anti-competitive consequences in circumstances beyond those

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[44] Ibid., s. 3.5.

> covered by these guidelines.[65]

Almost two decades later, the Canadian economist William Stanbury muses:

> I think there are consequences we do not really understand here. What worries me is that, for example, in the Bureau of Competition Policy, as far as I know, relatively little research is being done. There is no major inquiry under way to try to examine the consequences of this, and I would say this is a major omission.
>
> . . .
>
> I would be the first to say that very little economic theory could be brought to bear on aggregate concentration or conglomerate effects, although the performance of conglomerates has been studied quite extensively in the United States. Many of the advantages claimed for them do not show up in the empirical research--namely, that they are much more efficient and so forth and so on.
>
> . . .
>
> We know even less about the connections between the non-financial and the financial enterprises, the kind of thing that the Genstar-Imasco deal exemplifies. Remember before that we had Genstar acquiring Canada Trustco, and before that we had Genstar acquiring Canada Permanent, and now they are rolling them all into one.[66]

In reduced form,the debate concerning "pure" conglomerate mergers, and ultimately increased aggregate concentration, has polarized. One camp argues that competition laws ought to be governed by short-run considerations of consumer welfare maximization.[47] The opposing forces contend that antitrust laws should promote political and social goals. As Professor Bauer concludes:

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[65] Supra, n. 23, at s. III (20).
[66] Supra, n. 58, "Minutes of Proceedings", at p. 3:25.

> [T]he priority given to one of these two broad goals will in large measure determine one's attitude towards certain conglomerate mergers. The champion of the shortrun economic efficiency approach to antitrust will have no trouble with most, if not all, such transactions. The theories for challenging them are admittedly questionable and unproven on purely economic grounds. On the other hand, the exponent of the broader view of antitrust recognizes that many conglomerate mergers carry the potential for serious disruption of the business landscape, and that this has serious implications of an antitrust nature. Given this ambiguous evidence, an advocate of this second position will adopt the presumption that most large conglomerate acquisitions should be disallowed.[48]

Many experts agree with the latter position proposed by Professor Bauer. In a recent article reviewing the American experience, Preston concludes:

> [W]e have a lot of interproduct, interindustry, and

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[47] For the leading text on the goals of Canadian competition legislation, see: Paul K. Gorecki and W. T. Stanbury, The Objectives of Canadian Competition Policy, 1888-1983, Montreal: The Institue for Research on Public Policy, 1984. For a general discussion on the goals of antitrust laws, see also: D. Armstrong, Competition versus Monopoly: Combines Policy in Perspective, Vancouver, B.C.: The Fraser Institue, 1982; P. Areeda and D. Turner, Antitrust Law, Toronto: Little, Brown, 1978, at par. 103-113C; R. Bork, The Antitrust Paradox, New York: Basic Books, 1978, at pp. 50-89; C. Kaysen and D. Turner, Antitrust Policy: An Economic and Legal Analysis, Cambridge: Harvard University Press, 1959, at pp. 44-99; R. Posner, Antitrust Law, Chicago: University of Chicago Press, 1976, at pp. 8-35.

[48] J. Bauer, "Government Enforcement Policy of Section 7 of the Clayton Act: Carte Blanche for Conglomerate Mergers", (1983) 71 Cal. L. R. 348, at p. 371.

> intertype competition - firms going from one market area to the other all the time - and it's a major form of competition in our economy.
>
> . . .
>
> What we don't want to have happen though, is a single large firm dominating market after market.[69]

Professor Bauer concurs:

> First, they [1982 Guidelines] reflect a particular view of the goals of the antitrust laws that does not command universal approval. I view it as unfortunate that the new Guidelines look purely to the short-term economic consequences of the transaction, and dismiss as unimportant any social or political impact of a merger--including the loss or transfer of jobs and the increase in political influence, or the general effect of mergers on the corporate landscape.[70]

However, Baldwin and Gorecki arrive at a more neutral treatment:

> The merger process, in fact, "is not an aberrant one that is dramatically changing the structure of the manufacturing economy," they conclude. While merger activity does have competitive consequences, a broad policy either encouraging or discouraging it "is probably inappropriate," they add.[71]

Recent developments in Canada have heightened the awareness of academics and policy makers to the growing importance of conglomerate mergers, particularly acquisitions of financial enterprises by manufacturing and non-financial corporations. In a brief[72] submitted to the Legislative Committee reviewing the federal government's Green Paper, The Regulation of Canadian Financial Institutions, Mr. B. Ghert surveyed a number of the estimates of macro-concentration in the Canadian economy, and indicated the following general observations:

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[69] L. E. Preston, "Super-Concentration By Internal Growth Versus Merger: A 'Workable' World of 200 Giants (II)", (1984) 16 Antitrust Law and Economic Review 21, at p. 27.

[70] Supra, n. 68, at p. 370.

[71] Supra, n. 67. For an overview of the article, see: "Mergers can boost competition", (1986) 7 Au Courant 13. The above quote is excerpted from this overview.

(1) In 1981, the 100 largest non-financial enterprises accounted for 38% of sales, 50% of assets and 50% of profits,

(2) In 1983, the 15 largest non-financial enterprises accounted for 20% of all assets of all non-financial corproations,

(3) In 1983, the 7 largest financial enterprises plus the 6 largest chartered banks accounted for 36% of all assets of all financial corporations, and

(4) In 1984, 8 families and 2 management-controlled conglomerates accounted for over 35% of the TSE index.

In a concise summary, Mr. Ghert's concerns over conglomerate mergers and macro concentration highlighted by Professor Stanbury:

> (1) [A]bility to misallocate resources by restricting output and raising prices;

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[72] B. J. Ghert, "Brief on the Green Paper: The Regulation of Canadian Financial Institutions", Toronto: Cadillac Fairview Corp., 1985.

(2) [R]edistribution of income from the firm's customers to its owners;

(3) [F]irms with excessive power can become inefficient and wasteful;

(4) [A] high level of concentration reduces the number and diversity of decision makers in the economy;

(5) [L]arge concentrations may be unresponsive to regulatory agencies and have the ability to influence public policy;

(6) [C]orporate concentration may stimulate greater government intervention as a countervailing power.

(7) [U]se economic power to influence public policy via the political process, i.e., expenditures on lobbying, advocacy advertising, public relations, campaign contributions and have the ability to redirect corporate locational decisions.[73]

The first three cautions are strictly economic in nature, not unique to conglomerate mergers and have been reviewed at length under preceding discussions respecting the horizontal effects of all three basic forms of mergers. The remaining four warnings are of a political nature; analysis of these types of effects would not lend itself easily to the simple structural test advocated in the preceding sections of this paper. Of great concern is the potential impact that large "pure" conglomerate mergers might have on influencing public policy and inciting government intervention. Particularly if one subscribes to the view that the only effective long-run barriers to entry are government imposed, any incentive to aggravate the trend is undesirable. Furthermore, the efficacy of business lobby groups cannot be discounted.[74] Although these troublesome problems are not absent in non-conglomerate mergers, the ability to monitor these quasi-political aspects directly, rather than merely investigate the economic repercussions on competition resulting from horizontal mergers, may surpass the capabilities of economic technique. In the case of "pure" conglomerate mergers it is recommended hesitatingly that a "Cabinet override" appeal procedure to the Governor in Council be provided; this provision might rightly transfer the decision-making process to the political arena. Unfortuantely this device continues to sidestep the fundamental issue--by what standards should the Competition Tribunal evaluate conglomerate mergers?

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[73] Supra, n. 58, at p. 27.

Professor Stanbury in his testimony before the Legislative Committee on Bill C-91 has reached a similar resolution, but also eschews the issue of the appropriate substantive test to be applied:

> Here is a general approach with respect to conglomerates. First a new section of this act or a new act would require some kind of a threshold for review. In other words, we are not talking about nickel-and-dime operations; we are talking very large situations. So some kind of a threshold with respect to sales or

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[74] See: R. W. Phidd and B. Doern, The Politics and Management of Canadian Economic Policy, Toronto: McMillan, 1978, at p. 78; W. T. Stanbury, Business-Government Relations in Canada, Toronto: Methuen, 1986, at p. 244, for enlightening discussions on the effect of business lobbying in Canada.

> assets or number of companies involved, something of that sort.
>
> Second, Parliament needs to establish a set of criteria [emphasis added] against which to assess those mergers. Let me emphasize that the criteria proposed in the bill would be totally inadequate, the reason being that many of these things do not involve direct competition or vertical relationships. That is the definition of a conglomerate. But I think there are quite a number of criteria that Parliament would want to think about in this regard.
>
> Third, in my view it needs a public body to examine the evidence, to hold a hearing, to call forth executives, to ask experts to testify and so forth, to assess whether or not the merger should go forward. As I say, a public body. If you wish to delegate that to the competition tribunal, I think that would be a logical thing to do. But they would be operating under either a separate act, or separate part of the act with a separate set of criteria [emphasis added] regarding conglomerates.
>
> Fourth, in my view this body should make a public report to Parliament. You could have a variation here and say it should be without recommendations, merely assess the likely consequences of a conglomerate against the criteria, or it could be asked to make a recommendation. That is a matter of taste and so on. Finally, the Cabinet would decide, having had the public report, and the Minister responsible would make a statement in the House explaining the reasons for the decision.'[78]

Professor Stanbury's emphasis on disclosure in the process is proper; the practical implementation however may create significant difficulties. If the initial application is brought before the Competition Tribunal, it is recommended that matters involving political value judgments, legislative amendment and policy direction should not be dealt with in this forum. Consequently, the Director could present his case, relying solely on horizontal merger issues to sway the Tribunal in his favour. If the Director is unsuccessful, then at this juncture he could appeal to the Cabinet on the more amorphous grounds characterizing conglomerate mergers. Because an undertaking to publish the Cabinet decision and the reasons for the outcome would be a condition precedent to Cabinet review, one might well expect difficulties to arise at this stage of the process. The confidentiality of Cabinet deliberations would inevitably be raised to void such a condition. However, if Cabinet were given the authority to waive such confidence, then the political issues could be addressed, at Cabinet's option, in this more appropriate political forum. Conversely, if the confidentiality were not waived, then the Cabinet would be impliedly acquiescing to the Tribunal's decision to allow the merger. Ultimately, the decision of Cabinet would be reviewable by Parliament and the electorate, in theory.

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[78] Supra, n. 66, at p. 3:21-22.

The dearth of theories upon which to construct a framework for objectively appraising conglomerate mergers does not portend well for the usefulness of guidelines designed to trigger injunctive proceedings. If, as suggested by Professor Stanbury, a size of enterprise threshold is employed to guide the Director's decision, the problem of convincing the Tribunal to enjoin a "pure" conglomerate merger persists. Unless a policy of enjoining all large conglomerate mergers per se is acceptable, criteria to evaluate these increasingly prevalent mergers are still required, even at the provisional injunction stage. Proceeding under the presumption that the Tribunal should be restrained in its jurisdiction to judicially legislate public policy, it is submitted that the standard for preliminary appraisal of "pure" conglomerate mergers parallel the horizontal merger case. In essence, the Tribunal should assess the detriment to potential entry caused by the conglomerate merger in a highly concentrated primary market.

In the context of a broad programme of compliance to be instituted by the Director, merger guidelines for injunctive relief might increase the Director's leverage when persuading potential respondents to enter into undertakings. As has been recently witnessed in the Imasco takeover bid of Genstar, these informal agreements between the Director and the merging firms appear to be increasingly important.[74]

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[74] For an overview of Imasco's takeover bid for Genstar, Canada Trustco, and the issues raised when a manufacturing concern acquires a financial institution, see: Financial Times, 1986, April 7, April 14; Globe and Mail, 1986, March 25, April 18, 19.

E DEFENCES

1. INTRODUCTION

The American guidelines have consistently stressed two principal factors which could potentially affect the competitive significance of a particular firm's market share, the efficiencies and the failing company defence. In essence, these two defences are conceptually analogous; both investigate the costs arising from increased market power and the benefits accruing to social welfare if the merger is allowed to proceed.

The efficiencies defence has already been discussed in this paper under the subheading of horizontal mergers [Chapter C.3(e)]. The following analysis reviews the current state of acceptance of the failing company defence and its applicability to the Canadian setting.

The 1968 Guidelines downplayed the importance of economic economies as a defence to an otherwise anticompetitive merger. In general, the DOJ was of the view that economies should not prevail against a significant showing of harm to competition. For both horizontal and vertical mergers, the DOJ expressly stated that "unless there are exceptional circumstances" the Department would not accept as a justification for an otherwise challengeable merger the claim that the merger would produce economies.[1] The 1968 Guidelines on the other hand did permit defendants to raise the failing company defence under all three major types of mergers.[2] The two-part test was a codification of the judicial pronouncement in the International Shoe[3] case:

> A merger which the Department would otherwise challenge will ordinarily not be challenged if (i) the resources of one of the merging firms are so depleted and its prospects for rehabilitation so remote that the firm faces the clear probability of a business failure, and (ii) good faith efforts by the failing firm have failed to elicit a reasonable offer of acquisition more consistent with the purposes of Section 7 by a firm which intends to keep the failing firm in the market. The Department regards as failing only those firms with no reasonable prospect of remaining viable.[4]

The efficiency defence was accorded the status of a bona fide defence in the 1982 Guidelines. If the case were an extraordinary situation, the DOJ would weigh clear and convincing evidence of substantial cost savings from economies of scale as a "tie-breaker".[5] The failing company defence became extremely complex in the 1982 Guidelines, being severed unnecessarily into a separate approach for a failing firm and a failing division,[6] as well as a financially healthy subdivision of an allegedly failing parent firm.[7]

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[1] See: 1968 Guidelines, CCH Trade Reg. Rep., par. 10 and par. 16, for the rationale justifying this assertion.

[2] In the case of conglomerate mergers, the DOJ may deem it inappropriate to sue even though the acquired firm is not "failing" in the strict sense, if the case fell under section 18(a)(iii)(iv).

[3] See infra, n. 12, and accompanying text for a discussion of this landmark decision.

[4] 1968 Guidelines, supra, n. 1, at par. 9. See also, par. 15 and 21.

[5] See: Appendix ??, Defences, footnote 3, for a flowchart of the 1982 Economies Defence. Note that the "second best" doctrine, used to promote a search for a preferable purchaser under the failing company defence, is applied here also.

Following the historical trend, the 1984 Guidelines elevated the efficiency considerations from a strictly construed defence to a qualitative factor to be considered on an equal ranking with such factors as ease of entry and collusion.[8] The failing company defence, however, was retained in principle, with the noticeable deletion of the healthy division of a failing parent exclusion. Paralleling the 1982 version, the failing firm defence set forth a tripartite test for immunity:

> The Department is unlikely to challenge an anticompetitive merger in which one of the merging firms is allegedly failing when: (1) The allegedly failing firm probably would be unable to meet its financial obligations in the near future; (2) it probably would not be able to reorganize successfully under Chapter II of the Bankruptcy Act; and (3) it has made unsuccessful good faith efforts to elicit reasonable alternative offers of acquisition of the failing firm that would both keep it in the market and pose a less severe danger to competition than does the proposed merger.[9]

The fundamental addition to the test, which was noticeably absent in the 1968 edition, was the requirement that reorganization under the Bankruptcy Act[10] be unlikely.[11]

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[6] 1982 Guidelines, CCH Trade Reg. Rep., at par. 4502.20, s. V(B).

[7] Ibid., at footnote 57. See also: Appendix ??, Defences, footnote 2, for the outline of this defence.

[8] 1984 Guidelines, CCH Trade Reg. Rep., par. 4493.50, s. 3.5.

[9] Ibid., s. 5.1.

The following summary overview of the development and adaptability of the failing company defence will endeavor to highlight the evolution of the American jurisprudence, the emergent test of illegality, and the economic underpinnings of the defence. The discussion will then be redirected to review the brief inroads made by the defence into the Canadian legislation and to recommend an appropriate approach to such defences with respect to provisional injunctive guidelines.

2. THE AMERICAN JURISPRUDENCE

The failing company defence finds its genesis in the 1930 International Shoe[12] case. The Court found that the failing company defence would apply when there was a "grave probability of business failure" coupled with "no other prospective purchaser":

> In the light of the case thus disclosed of a corporation with resources so depleted and the prospect of rehabilitation so remote that it faced the grave probability of a business failure with resulting loss to its stockholders and injury to the communities where its plants were operated, we hold that the purchase of its capital stock by a competitor (there being no other

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[10] Bankruptcy Act, 11 V.S.C. 1101 (1982).

[11] This secnod criterion was a codification of the ratio laid down in the Citizen Publishing case, infra, n. 14.

[12] International Shoe Co. v. FTC, 280 U.S. 291 (1930).

> prospective purchaser), not with a purpose to lessen competition, but to facilitate the accumulated business of the purchaser and with the effect of mitigating seriously injurious consequences otherwise probable, is not in contemplation of law prejudicial to the public interest and does not substantially lessen competition or restrain commerce within the intent of the Clayton Act.[13]

In sum, the defence consisted of two elements: (1) the failing company condition and (2) the preferred purchaser negation.

The definition of a failing company was refined by the Supreme Court in the Citizen Publishing[14] case:

> [W]e know from the broad experience of the business community since 1930, the year when the International Shoe case was decided, that companies reorganized through receivership, or through Chapter 10 or Chapter 11 of the Bankruptcy Act often emerged as strong competitive companies. The prospects of reorganization of the Citizen in 1940 would have to be dim or nonexistent to make the failing company doctrine applicable to this case.[15]

Areeda and Turner speculate that merely dim prospects for reorganization should not satisfy this criterion. As the learned authors state:

> It would make little sense to require proof in all cases that a merging firm not only faces insolvency or bankruptcy proceedings but has no reasonable prospects of surviving them as a speculative issue into merger litigation. It would force firms to take the reorganization route whenever the only prospective acquirers are barred by presumptions of illegality

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[13] Ibid., at p. 302-303.

[14] Citizen Publishing Co. v. United States, 394 U.S. 131 (1969).

[15] Ibid., at p. 138.

based on market shares.[16]

With respect, it appears that the reorganization criterion is merely a subset of the third element, namely, the probable existence of a less offensive remedy.

The proof of the absence of a preferred purchaser should depend upon the degree of harm resulting from the merger. Recognizing the limitations inherent in formulating tests for presumptive illegality, Areeda and Turner suggest that the failing company defence be deemed established:

(1) by proof that a firm is "failing" where
  (a) one merging firm's market share does not exceed 5 percent and the other's 50 percent; or
  (b) the merging firms' aggregate share does not exceed 20 percent, and the four-firm concentration ratio after the merger would not exceed 75 (or 70) percent.
(2) by further proof that there are no "preferred purchasers" where
  (a) one firm's market share does not exceed 10 percent, and the other 55 percent; or
  (b) the merging firms' aggregate share does not exceed 40 percent, and the four-firm concentration ratio after the merger would not exceed 90 (85) percent.
(3) by further proof that the firm faces liquidation.[17]

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[16] P. Areeda and D. Turner, Antitrust Law, Toronto: Little, Brown, & Co., 1980, at par. 926b.

[17] Ibid., at par. 927a.

The foregoing thresholds presuppose the definition of a "preferred purchaser". The authors propose the following definition of a "preferred purchaser" as one:

(1) who would remain in the market;

and

(2) whose acquisition would be lawful
(a) even if the acquired firm were not failing, or
--
(b) simply on proof that the acquired firm was failing, providing its market share is at least five percentage points below that of the proposed acquirer;

or,

if there are no such purchasers,

(3) who is not presently a competitor, or, if there are no such purchasers, a competitor whose market share is at least five percentage points below that of the proposed acquirer.[18]

The intention of the alternate acquiring firm to remain in the market would ensure that the new purchaser would not withdraw the failing firm's assets from the market and utilize them elsewhere; the consequences of this tactic would be tantamount to liquidation. This continuation factor will dominate the discussion *infra* which considers whether the failing comapny should be required to exit the market, rather than merger, in order to minimize social welfare losses.

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[18] *Ibid.*, at par. 928a.

The onus lies on the defendant to prove that a reasonable search has been conducted; the firm must make a "sufficiently clear showing [that it] undertook a well conceived and thorough canvass of the industry such as to ferret out viable alternative partners for a merger.[19] In this regard, the purchaser need not be classified as "preferred" if the offer is unreasonably low[20] or "piecemeal"[21] The failing subdivision defence is, in theory, simply a scion of the basic defence; if the division would be liquidated if not sold, and bona fide efforts have failed to secure alternate purchasers, then the defendant may invoke this shield.[22] This specialized exemption, although applied at the lower court level,[23] has not been considered in the Supreme Court. Some commentators have argued that the failing company defence has been broadened to encompass what might be described as a "weakened" company defence.[24] At this point, the discussion enters the realm of erudite conjecture.[25]

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[19] U.S. v. Pabst Brewing Co., 296 F. Supp. 944 (E.D. Wis 1969), at p. 1002.

[20] Areeda & Turner, supra, n. 16, at par. 930.

[21] Ibid., at par. 931.

[22] See: Areeda & Turner, Ibid., at par. 926e for a distinction between the main test and the failing division special case. The authors argue that the debt-equity ratio may be artificially enhanced in order to invoke the defence.

[23] See: FTC v. Great Lakes Chemical Corp., 528 F. Supp. 84 (N.D. Ill. 1981).

[24] See: U.S. v. General Dynamics Corp., 415 U.S. 486 (1974); U.S. v. International Harvester, 564 F. 2d 769 (7th Cir. 1977).

It is vital to emphasis as the conclusion to the foregoing introductory review of American common law, that the American courts are applying an absolute or per se defence. Moreover, the 1984 Guideliens envision a similar application; the Guidelines do not offer the possibility of a balancing procedure to weigh the costs and benefits. Is an absolute defence justified on economic grounds? Does the Competition Act contemplate a similar provision? Moreover, should the Canadian guidelines emulate their American counterpart? These questions will be addressed in the subsequent three sections of this chapter.

3. ECONOMIC BASIS FOR THE FAILING COMPANY DEFENCE

As a general approach to defences, and one which has not been employed as such in the antitrust and competition policy literature, the opportunity costs of the various options may be ranked, the least costly alternative indicating the proper choice. The difficulty has always been to estimate the associated costs. Oliver Williamson, in his now well-respected article on economies as an antitrust defence,[26] illustrates the balancing concept for the case of a merger which also realizes economies of scale. In this situation, the opportunity costs of permitting the merger, measured by the dead weight social loss to society, are balanced against the opportunity costs of prohibiting the merger, these costs being manifest by the increase in producer surplus accruing to the producer as a result of lower average costs. The option with the lower opportunity cost will identify the preferred policy objective.

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[25] See: Areeda & Turner, supra, n. 16, at par. 934, 935 for a comprehensive discourse.

[26] See: Appendix I for the development of Williamson's thesis.

Following a similar analysis, one can pose the question of opportunity costs when the failing company argument is adducted. The preliminary question should only address what the potential effect on competition would be if the merger were to proceed. On first blush, one might perceive that a company that is failing would contribute little to competition and its disappearance via merger as an independent competitor could hardly impair competition. As might be suspected, this view is too simplistic. If the firm were to exit the market, rather than merge, fringe competitors may be afforded an opportunity to pick up the excess demand. As Areeda and Turner note:

> If the merger is prevented, the failing firm's customers might disperse along the lines of existing market shares. In that event, the larger the share of the proposed acquirer, the less would be the competitive gain from preventing the merger.[37]

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[37] Areeda & Turner, supra, n. 16, at par. 925, footnote 1.

With respect, this result would only occur if all the marginal cost curves were horizontal. Additionally, the failing firm may be capable of surviving a bankruptcy reorganization, the opportunity costs of this approach being less than those arising from the merger.[18]

As a general procedure in these cases, it is recommended that the substantive issue always be addressed: Is the merger likely to lessen competition substantially. It is quite conceivable that the acquisition of the failing enterprise, even if it were healthy, would have no adverse competitive effects. If the opportunity cost anlaysis indicated that the merger would likely promote competition, or retain the status quo, then the analysis would not need to proceed further.

The second criterion would evaluate the trade-off between increased market power on the one hand and reduced productive capacity on the other. The failing company is faced with two alternatives: it may merge with the acquiring firm or exit the market. The decision to exit the market would result in the assets of the failing firm being sold as scrap or being utilized in less-efficient "second-best" production. From a social welfare perspective, the tradeoff may be evaluated by weighing the social welfare loss realized when the firm exists in contrast to when the firm merges.

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[18] See: Citizen Publishing case, supra, n. 14, and the discussion accompanying.

In the case of firm exit, the supply in that particular market will necessarily fall, which will in turn precipitate a drop in economic surplus. Conversely, if the failing firm were to merge, the supply would remain constant, or at least not fall as significantly; however, the output level would diminish and prices would rise. Again, the normal dead weight social loss would develop. Most commentators have failed to consider the negative economic surplus which would result if the failing firm were to exit. The unenviable task of antitrust policy is to weigh the corresponding impacts on the economy.

Shughart and Tollison[33] endeavor to determine which course of conduct creates higher welfare losses, exit or merger. In simplied form, they argue that the marginal cost curve, acting as a proxy for supply, will intersect the marginal revenue curve farther to the right in the case of the merger. "Accordingly, the deadweight loss from the merger is less than the loss obtaining [sic] when the failing company exists from the industry".[30] The merger alternative leads to the least restrictive output level and consequently the smallest welfare loss. As the authors summarize:

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[33] W. F. Shughart and R. D. Tollison, "The Welfare Basis of the 'Failing Company' Doctrine", (1985) 30 Antitrust Bulletin 357.

> When one of the incumbent firms in a two-rival industry fails, the surviving company enjoys a short-run monopoly in any case-scrapping of the failed firm's assets, sale to a buyer outside the industry, or merger-but the acquisition option leads to the smallest output restriction, and therefore entails the smallest welfare loss. For this reason the failing firm doctrine is valid in the sense that purchase of the failing company's assets by its former competitor is preferable to the alternatives.[31]

Although the test enunciated in International Shoe and Citizen Publishing, and codified in the 1984 Guidelines, reaches the same end, the costs incurred in investigating the probability of business failure and the burden imposed on the failing firm to undertake bona fide efforts to find the preferred purchaser create unwarranted social costs. The implication for public policy is expressed by the authors:

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[30] Ibid., at p. 361. The author's argument is summarized in the following passages found at pp. 360-361:

> We first suppose that the proposed merger is blocked and that the assets of Firm 2 are auctioned off to alternative uses. Firm 1 now faces the market demand curve and chooses the price-output combination consistent with profit maximization. There is the usual deadweight loss associated with monopoly.
>
> ~~We treat~~ the second option posed by the failing firm doctrine, merger, as a multiplant monopoly problem.
>
> . . .
>
> In our example, Firm 1 again faces the market demand curve. If the surviving company were to purchase the assets of Firm 2, the output of the merged firm would necessarily exceed the output Firm 1 would produce without acquiring Firm 2. This follows immediately by noting that, given the same demand and marginal revenue schedules, the intersection of marginal revenue with the horizontal sum of the two firms' marginal cost curves lies to the right of the intersection of marginal revenue with Firm 1's marginal cost curve alone.

[31] Ibid., at p. 362.

> [B]ecause the failing company doctrine is justifiable on welfare grounds, the defence should be applied expeditiously. Mergers between failing firms and their former rivals should go through with minimal delay.[32]

It is submitted that Shughart and Tollison's policy recommendations are based on the assumption that the acquiring firm will maintain the production at least in part, of the failing firm subsequent to the merger. If the acquiring firm's intentions were to eliminate a disruptive competitor, rationalize its own capacity, or create a monopolistic position, then the inference that the merger route is superior is rebuttable. Simiarly, if the failing company were to exit and the residual demand disproportionately distributed to the dominant firm, the results obtained by Shughart and Tollison might again be contestable. Although an absolute defence is not desirable, the approach proposed by Shughart and Tollison does not appear to vary greatly in substnace from just such an approach. The objective of balancing the costs of exit versus merger is commendable; the policy recommendation to favour the merger route may be premature.

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[32] Ibid., at p. 364.

As an offshoot of the judgement in International Shoe, the American commentators have pondered whether the public interst in maintaining competition should be weighed against possible detrimental effects to private interests if the failing company were allowed to exit. The social costs to shareholders and employees, the potential for increased unemployment and decreased supplier revenue have all been proposed as possible counterweights to the possible anticompetitive consequences of exit. However, the costs of business failure, to all the affected parties, are usually internalized, rendering such analysis extremely remote. Furthermore, even if the cost values were available,

> [I]t seems neither feasible nor appropriate for courts to determine and choose among conflicting private interests in the context of the failing company defense to a merger. The effects of the various alternatives on the various private interests would often be largely indeterminate. And there are countervailing considerations. For example, the acquiring firm that would move the acquired operations elsewhere would do so for efficiency reasons. Moreover, while one might conceive of some hierarchy of weights for the various conflicting interests-based on efficiency, the desirability of encouraging risk-taking, and the like-it would be difficult if not impossible to avoid debatable value choices, unpredictability, and diverse legal results.[33]

In the final analysis, a comparison of the private interests and public concerns is not feasible because the two variables are measuring noncomparable or uncommensurable units. In the American jurisprudence, "the Supreme Court has often held that in formulating a remedy for antitrust violations, effective relief takes priority over harm to private interests".[34] The DOJ's view, as expressed in the 1982 Guidelines, parallels the courts in this respect:

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[33] Areeda and Turner, supra, n. 16, at par. 925b.

> Although its original basis is open to question, the [failing company] defense is sometimes explained as a balancing of competitive and non-competitive concerns. Under that view, when the elements of the defense are satisfied, there is a conclusive presumption that the anticompetitive dangers associated with the merger are outweighted by the income losses to creditors, stockholders, and communities associated with the failure of the firm. As a general matter, the Department views the incorproation of non-competitive concerns into antitrust anlaysis as inconsistent with the mandate contained in the antitrust laws. To the extent that the financial health of the firm is relevant to the competitive analysis, the Department, of course, will consider it in that context.[35]

The student of the failing company defence is led to the inescapable conclusion that an absolute defence or per se rule is not consistent with contemporary economic thinking; a "rule of reason" is better suited to balance the net benefits arising from both the merger and exit by the failing firm. This "weighscale" approach is analogous to the general technique employed in the 1984 Guidelines and the Canadian Competition Act[36] to examine efficiencies; all criteria omit any reference to absolute standards, inferences, presumptions and thresholds. While preferred in economic circles, the balancing required to determine the issue places an onerous burden on the adjudicative body to rank the inevitably conflicting expert evidence. Even if the court were to rely on Shughart and Tollison's policy recommendation, expectations on the future production level of the failing firm, post merger, are indeed tenuous. In short, the proguosis for the post-merger level of competition is no more determinative in the case of a failing company than it is in the case of a healthy one.

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[34] Ibid., at par. 925c.

[35] 1982 Guidelines, supra, n. 6, at par. 4505.20, s. V(B), footnote 54.

[36] See: Competition Act, S.C. 1986, s. 68 for the Canadian version of the efficiency defence.

4. THE FAILING COMPANY DEFENCE IN CANADIAN LEGISLATION

The failing company defence was conspicuously absent in the Stage I Amendments to the former Combines Investigation Act. In the precusor to the Stage II Amendments, the Skeoch-McDonald Report[37] proposes a failing company exemption to substantive merger proscriptions, but the exemption should not be automatic:

> If the industry were contracting and the process of adjustment required that some firms should be eliminated, the process of cost and price adjustment might very well be hindered if another firm were to

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[37] Skeoch, L.A. and McDonald, B.C. et. al., Dynamic Change and Accountability in a Canadian Market Economy, Ottawa: Supply and Services Canada, 1976.

enter by the merger route.[38]

The two Stage II proposals in 1977 for legislative amendment did address the issue of the failing company defence. Both Bill C-42 and Bill C-13 proposed that in determining whether or not a merger lessened competition substantially, the Competition Board shall have regard to:

> (n) any likelihood that a firm that is a party to a merger or proposed merger was or is about to fail.[39]

Several observations must be noted in passing. First, the Board was compelled to considered the failing company doctrine. However, it need only "have regard to" the principle; no legal interpretationof this phrase has yet been enunciated by the courts. The legislative directive appears mildly schizophrenic, the Competition Board has no discretion to ignore the defence yet the magnitude of its significance is subject to the Board's discretion. The use of the word "any" is unpredictable when contrasted with the insertion of the definite article "the". Furthermore, one interpretation of the phraseology might suggest that a firm that was about to fail, but is now solvent and viable, is protected by the exemption. Finally, there is no provision for the failing division scenario.

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[38] Ibid., at p. 87. The report also makes reference to a structural rationalization exemption (p. 87):

> Indeed, more detailed investigation might indicate that a merger could contribute to the erosion of entry barriers and to speeding up the process of change. Such situations should not be regarded as exceptional, although it does not appear possible to identify them adequately in a preliminary analysis.

[39] Bill C-42, Competition Act, March 1977, s. 31.71(4)(n).

Bill C-29 addressed the failing company question[40] and rectified the ambiguous wording set forth in its predecessor. The failing division exemption was included and the potential for misinterpretation minimized. The issue continued to be treated not as a true defence, but merely as a factor to be considered in determining whether competition had been lessened significantly.

The new Competition Act has adopted the identical wording in Bill C-29, save for one significant modification:

> 65. In determining, for the purpose of section 64, whether or not a merger or proposed merger prevents or lessens, or is likely to prevent or lessen, competition substantially, the Tribunal may have regard to the following factors:
>
> > (b) whether the business, or a part of the business, of a party to the merger or proposed merger has failed or is likely to fail;[41]

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[40] See: Bill C-29, An Act to Amend the Combines Investigation Act, 32-33 Eliz II, 1983-1984, s. 31.74(1)(a), which reads:
31.74 (1) In determining, for the purpose of section 31.72, whether or not a merger or proposed merger prevents or lessens, or is likely to prevent or lessen competition significantly, the court shall have regard to the following factors:
(a) whether the business, or a part of the business, of a party to the merger or proposed merger has failed or is likely to fail;

[41] Competition Act, S.C. 1986, s. 65 (b).

The adjudicative Tribunal now has complete discretion to disregard the issue entirely. With respect, the use of the imperative "shall" would seem more appropriate; the Tribunal must have regard to the defence, if raised, but the weight to be afforded such evidence would still lie with the Tribunal.

5. THE FAILING COMPANY DEFENCE IN MERGER GUIDELINES

Due to the inclusion of the factor in the Competition Act, the Director would be remiss in neglecting to regard a strong case of a failing company when determining whether to apply for an order pursuant to the substantive provisions set forth in section 64 of the Competition Act. The counsel is not as straightforward when the matter involves an application for provisional relief under S.72 or S.76 of the Competition Act.

The Canadian test will undoubtedly not be an absolute defence; the Tribunal will ultimately be engrossed in a complex process of cost-benefit analysis. As a consequence, at the prelimniary stage, it is recommended that the injunctive guidelines overlook such involved considerations. Paralleling the discussion on efficiencies, this is not to advocate the omission of such deliberations on the trial of the merits.

X CONCLUSIONS

The Competition Act has been heralded as radically reforming merger legislation, and has thereby generated considerable optimism. However, a thorough and impartial examination of the new merger provisions has in fact identified many potential pitfalls and limitations, perhaps with the result of dampening this premature enthusiasm.

The major area of difficulty remains the substantive test. Although the Act includes extensive modifications to the substantive test which address the criticisms raised respecting the criminal burden of proof and the "detriment test", other debilitating conditions persist. The "substantial lessening" criterion remains problematic and will almost certainly rekindle debate over the meaning of "detriment" and over the interpretation and measurement of "rivalry". In conjunction with these issues, the "efficiencies defence" cannot help but thrust the entire evaluation process into a complex analysis of the foreseeable costs and benefits of the merger. As well, the standard for review may conceivably have been reduced to its former status as a result of directing the adjudicative body to consider whether effective competition would remain. On balance, these factors seem to effectively nullify what is perceived to be a more restrictive anti-merger policy.

The omission of any attempt to deal with the matter of relevant market delineation is difficult to understand and worrisome. Particularly in light of the general predilection to construe "competition" in the traditional restricted sense, it is submitted that bridging this legislative lacuna will be crucial to the operation of the provisions.

On the positive side, the current Act does not preclude a broader jurisdiction than was intended. A liberal reading of the statute alone does not appear to preclude the review of "pure" conglomerate mergers. This hypothesis has been discussed in chapter IX D. Although the intentions expressed by the then Minister of Consumer and Corporate Affairs were to tailor the merger provisions to deal with the horizontal effects of horizontal and diversified mergers, acceptance of a broad interpretation of the term "competition" will bring conglomerate mergers within the confines of the Act. This extended sphere of influence could increase the Act's usefulness in dealing with aggregate economic concentration. It must be emphasized that it is very unlikely that such a forward-looking approach to the new Act will actually be adopted.

Another fundamental amendment to the former Act establishes a complex procedure of merger pre-notification. With respect to this "Canadianized" version of the Hart-Scott-Rodino pre-notification provisions, a tentative conclusion would characterize them as extremely complex but otherwise useful. As Edward Greenspon has indicated:

> The bureau is not interested in overburdening business by seeking pre-notification in all mergers, he said. Internal practice runs on past deals suggest that these thresholds would catch about two-thirds of the cases for which officials think "a significant issue" is raised by a merger.
>
> The Government might be alerted to others by public complaints.'

Of course, the question of what constitutes "a significant issue" remains unanswered. After reviewing the provisions, it appears that problems with transactional neutrality and the timing of the notification do exist. As well, the notification requirement may not be suitable to hostile takeovers. The ultimate effectiveness of the pre-merger notification requirements will depend to a great extent on the procedures enacted in the forthcoming regulations.

The examination of the availability of provisional injunctive relief has revealed two convincing propositions. First, the real battle to halt an undesirable merger will be fought at the injunction stage. Secondly, the success of an application for either a preliminary injunction to extend the pre-notification "waiting period" or an interlocutory injunction to enjoin the transaction will be contingent upon the strength of the applicant's case. In order to avoid having the Tribunal try the case on its merits at this preliminary stage, it is recommended that both types of injunctions be construed in a manner which would impose a

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' Edward Greenspon, "Federal tribunal sets new stage for mergers", August 18, 1986, Globe and Mail B1.

burden of proof somewhat lower than the customary civil burden of proof.

The provisional injunctions provided in sections 72 and 76 of the Competition Act ought to fulfil a role similar in principle to the preliminary hearing in a criminal case. On application an inference should be established that the merger has breached the substantive provisions. As in the case of the preliminary hearing, the Tribunal should be "required to decide after taking the evidence, whether or not there is sufficient evidence to put the accused on trial".[3] At the injunction stage, the Tribunal should not determine the issue; the Tribunal is not dealing with the preponderance of evidence. However, as Salhany states, there must be more than a "mere possibility or suspicion" that the provision has been breached. The practical test, which has been suggested for the preliminary hearing in a criminal case, is for the judge to decide whether, at trial, the case would be submitted to the jury. Under an injunction application, this test would determine the availability of temporary relief. The crucial importance of injunctive relief within the scheme of the Act has been emphasized in this paper and should not be undermined by anything less than a determined effort to categorize the burden of proof in an effective manner.

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[3] R.E. Salhany, Canadian Criminal Evidence, Toronto: Canada Law Book, 1978.

The final area investigated is the potential for developing administrative merger guidelines. Essentially, the 1984 U.S. Merger Guidelines adopted by the Department of Justice are a precis of the relevant issues which the DOJ will consider and of the accepted economic thought which it will apply when determining whether or not to proceed under section 7 Clayton Act against the parties to the merger. Although a similar "flowchart" is recommended for use in Canada by the Director, this paper counsels that a truncated and less unpredictable version could be developed for use in determining the appropriateness of provisional injunction applications by the Director. An officer of the Department of Consumer and Corporate Affairs has intimated that, although Canadian guidelines may not be as clear cut as their American counterparts, "[i]t's possible there may be something at a latter date."[3]

In summary, one must question whether the merger provisions in the Competition Act in fact actually are a radical departure from their predecessors. It is conceded that, on balance, they are at least no less effective than the former proscriptions. However, there is mounting evidence that not even the unfettered profit-motivated parties themselves can predict a successful merger.[4] This inherent inability to "choose the winners" does not bode well for the prospects of the Tribunal.

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[3] Supra, n. 1.

This entire study has assumed that at least some large mergers are accompanied by undesirable effects on social welfare. Lingering doubts persist concerning both the economic relevance and the actual effectiveness of government intervention to improve upon the merger decisions of independent, profit-maximizing enterprises which have a vested interest in the success of the venture.

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[4] Edward Greenspon, "Takeover gluttons face indigestion risk", August 16, 1986, Globe and Mail B1.

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APPENDIX A

THE CHRONOLOGICAL DEVELOPMENT OF THE LEGISLATION

TABLE I

Combines Investigation Act, S.C. 1978, c.C-23, as am.

I. ADJUDICATION
  1. Court v. Tribunal
    -S.44(2) Superior Court of Criminal Jurisdiction under Criminal Code
    -S.46(1) Federal Court-Trial Division; S.46(a) with consent
  2. Powers of Tribunal/RTPC/DIR
    -S.45(2) documentary evidence
    -S.45.1 statistical evidence
    -S.46.1 compliance with Commission Orders
    -S.47 DIR general inquiry
    -S.17 Oral Exam.
    -S.18 Part V Hearing
    -S.19 Reporting
  3. Civil v. Criminal
    -S.44(1) Procedure as indictable offence under Criminal Code

II. INVESTIGATION
  4. Search and Seizure
    -S.9 Require Written Submission of any Information
    -S.10(1) Entry of Premises
    -S.10(3) DIR requires certificate of RTPC
    -S.11 Copies
    -S.12 Affidavits
    -S.17 Compel Witnesses and Production of Documents

III. MERGER TEST
  5. Horizontal
    -S.2 Competition
  6. Vertical
    -S.2 Supplier or customer
  7. Conglomerate
    -S.2 Any other person
  8. Structure
    -S.2 "Competition is, or is likely to be lessened"
      (common law results)
  9. Conduct
    n/a
  10. Performance
    -S.2 "to the detriment or against the interest of the public"
  11. Economies Defence
    -S.2 Included in "detriment to public"
  12. Failing Company Defence
    n/a
  13. Relevant Market
    n/a
  14. International Mergers
    n/a

IV. PRE-MERGER REQUIREMENTS
  15. Registration
    n/a
  16. Pre-Clearance
    n/a
  17. Pre-Notification
    n/a

V. REMEDIES
  18. Fines
    -S.30 discretion
  19. Prison
    -S.30 - 2 years
    -S.33 - 2 years
  20. Patents
    -S.29 "lessen, unduly, competition"
  21. Tariffs/Quotas
    -S.28 applies to articles
      Cabinet may reduce
  22. Orders: Divest, Dissolve, Prohibit
    -S.30(1) Ex post Part V conviction
      (a) cease and desist
      (b) dissolution
    -S.30(2) Ex ante part V conviction
      (a) cease and desist
      (b) dissolution
  23. Conditional Orders
    n/a
  24. Final Orders
    -S.31 Required under Part V Conviction to Report up to 3 years
  25. Damages
    -S.31.1 single damages plus costs; 2 year limitation
  26. Publications
    -S.49 Director's Annual Report
    -S.19 Part V Reporting
  27. Interim Injunctions
    -S.29.1 has done, is about to, is likely to
      constituting or directed toward offence Part V, 46.1
      -AND-
      offence cause injury to competition which cannot be
      remedied under other section
      -OR-

      Injury cannot be remedied otherwise and injury to
      Plaintiff substantially greater than to Defendant if no
      offence proven pending S.30(a) prosecution

VI. APPEALS
  28. Appeals
    -S.46(3) to Federal Court Appeal Division, then S.C.C.

VII. MISCELLANEOUS
  29. Intent
    -S.33 "knowingly"
  30. Class Actions
    n/a
  31. Provincial Coordination
    n/a

TABLE 2

1969 Economic Council of Canada: Interim Report on Competition Policy

I. ADJUDICATION
- 1. Court v. Tribunal
  - p. 109
  - a) Special Judges to Exchequer Court
  - b) Tribunal "Competitive Practices Tribunal"
  - 7 members
  - absorb functions of RTPC
- 2. Powers of Tribunal/RTPC/DIR
  - n/a
- 3. Civil v. Criminal
  - Civil p. 107

II. INVESTIGATION
- 4. Search and Seizure
  - n/a

III. MERGER TEST
- 5. Horizontal
  - any class of merger
- 6. Vertical
  - any class of merger
- 7. Conglomerate
  - p. 117 - little experience
- 8. Structure
  - "Substantial economic importance"
  - p. 116 Shopping List
  - a) degree of control
  - b) history of acquire
  - c) market shares etc.
- 9. Conduct
  - n/a
- 10. Performance
  - "significant potential for harm" to final consumer v. benefit p. 115
  - (8) substantial "social savings" in use of resources, p. 116
- 11. Economies Defence
  - Included in Test
  - "substantial social savings" i.e. savings in resources
- 12. Failing Company Defence
  - n/a
- 13. Relevant Market
  - n/a
- 14. International Mergers
  - n/a

IV. PRE-MERGER REQUIREMENTS
- 15. Registration
  - registration, p. 115
  - voluntary v. mandatory
- 16. Pre-Clearance
  - n/a
- 17. Pre-Notification
  - n/a

V. REMEDIES
- 18. Fines
  - p. 191 - continue
- 19. Prison
  - p. 191 - continue
- 20. Patents
  - n/a
- 21. Tariffs/Quotas
  - n/a
- 22. Orders: Divest, Dissolve, Prohibit
  - p. 191 - continue
- 23. Conditional Orders
  - conditional acceptance, p. 114
- 24. Final Orders
  - n/a
- 25. Damages
  - single damage suits, p. 191
- 26. Publications
  - publicize p. 113
- 27. Interim Injunctions
  - ECC Interim Injunction, p. 115

VI. APPEALS
- 28. Appeals
  - from Tribunal to Courts, p. 113

VII. MISCELLANEOUS
- 29. Intent
  - n/a
- 30. Class Actions
  - n/a
- 31. Provincial Coordination
  - n/a

TABLE 3

1971 Bill C-256

I. ADJUDICATION

1. Court v. Tribunal
   -S.3 Competitive Practices Tribunal
   -S.11 Commissioner (old DIR)
2. Powers of Tribunal/RTPC/DIR
   -S.45 Advance Rulings
   -S.44 Guidance Rules
   -S.67 Initiation of Inquiry Minister, Comm., 6 citizens, A.G.
   Part IX - Evidence; S.46 General Inquiry
3. Civil v. Criminal
   Mergers, civil

II. INVESTIGATION

4. Search and Seizure
   n/a

III. MERGER TEST

5. Horizontal
   n/a
6. Vertical
   n/a
7. Conglomerate
   n/a
8. Structure
   -S.34 -TEST - any merger challenged if lessens competition significantly that would have existed
   -Factors to consider (as defences)
   -S.35 -International Mergers
9. Conduct
   n/a
10. Performance
    n/a
11. Economies Defence
    -S.34(3) significant improvement in efficiency passed on to public in lower prices
    -S.34(5) Factors to consider
12. Failing Company Defence
    n/a
13. Relevant Market
    n/a
14. International Mergers
    -S.35

IV. PRE-MERGER REQUIREMENTS

15. Registration
    -S.32(1) merger where assets or sales greater than $5 million must be registered before or within 2 weeks after merger
    -S.32(4) limits Tribunal challenge to 1 year
    -S.33 all foreign takeovers must register
    -S.34 TEST
    -S.35 Advance Rulings
16. Pre-Clearance
    n/a
17. Pre-Notification
    n/a

V. REMEDIES

18. Fines
    -S.74(3) Failure to comply with SS.32,33
    $10,000 plus $1,000/day
19. Prison
    1 year
20. Patents
    -S.51
21. Tariffs/Quotas
    -S.53
22. Orders: Divest, Dissolve, Prohibit
    -S.34(1) prohibit/dissolve
    -S.36 prohibit interlocking directorships
23. Conditional Orders
    -S.34(2) conditional acceptance
24. Final Orders
    n/a
25. Damages
    -S.55 double damages for breach of order
    -S.80 double damages only for restricted practices, not merger
26. Publications
    n/a
27. Interim Injunctions
    -S.47 Interim Injunction by Comm. if:
    a) obtained or may be able to obtain evidence for prohibition
    b) *and* in public interest

VI. APPEALS

28. Appeals
    Federal Court Act - appeal from Tribunal

VII. MISCELLANEOUS

29. Intent
    -S.34(4)(c) intent to reduce competition
30. Class Actions
    n/a
31. Provincial Coordination
    n/a

TABLE 4

1973 Bill C-227; C-7; C-2 Stage I Amendments (1976) enacted

I. ADJUDICATION
- 1. Court v. Tribunal
  - n/a
- 2. Powers of Tribunal/RTPC/DIR
  - -S.2 product includes article and service (service means service of any description)
  - -SS.4,4.1 exceptions
- 3. Civil v. Criminal
  - n/a

II. INVESTIGATION
- 4. Search and Seizure
  - n/a

III. MERGER TEST
- 5. Horizontal
  - n/a
- 6. Vertical
  - n/a
- 7. Conglomerate
  - n/a
- 8. Structure
  - n/a
- 9. Conduct
  - n/a
- 10. Performance
  - n/a
- 11. Economies Defence
  - n/a
- 12. Failing Company Defence
  - n/a
- 13. Relevant Market
  - n/a
- 14. International Mergers
  - n/a

IV. PRE-MERGER REQUIREMENTS
- 15. Registration
  - n/a
- 16. Pre-Clearance
  - n/a
- 17. Pre-Notification
  - n/a

V. REMEDIES
- 18. Fines
  - n/a
- 19. Prison
  - n/a
- 20. Patents
  - n/a
- 21. Tariffs/Quotas
  - n/a
- 22. Orders: Divest, Dissolve, Prohibit
  - n/a
- 23. Conditional Orders
  - n/a
- 24. Final Orders
  - -S.46.1 Failure to comply with RTPC order
- 25. Damages
  - -S.31.1 single damages + cost
    2 year limit
- 26. Publications
  - n/a
- 27. Interim Injunctions
  - -S.29.1 Interim Injunctions added

VI. APPEALS
- 28. Appeals
  - n/a

VII. MISCELLANEOUS
- 29. Intent
  - n/a
- 30. Class Actions
  - n/a
- 31. Provincial Coordination
  - n/a

TABLE 5

1976 Skeoch-McDonald Report Dynamic Change and Accountability in a Canadian Market Economy

I. ADJUDICATION
- 1. Court v. Tribunal
  - -p.289 eliminate RTPC
    replace with tribunal
  - -p.293 "National Markets Board"
- 2. Powers of Tribunal/RTPC/DIR
  - -p.298 Independent
  - -S.31.4(2) C.I.A. type powers to grant orders
- 3. Civil v. Criminal
  - -p.89,39 "reasonable probabilities"
    functional test
    civil
  - -p.316 criminal to civil

II. INVESTIGATION
- 4. Search and Seizure
  - n/a

III. MERGER TEST
- 5. Horizontal
  - -p.80 may create Case I/Case II oligopoly
- 6. Vertical
  - -p.81 creates Case II oligopoly
- 7. Conglomerate
  - -p.82,83 Diversification
    Conglomerate
    Investment
    may be Case II
- 8. Structure
  - -p.71 primary merger consequence = artificial restraints
    secondary merger consequence = real-cost economy
  - -p.79 Stage I: Identification
    (a) pertinent market
    (b) market power
- 9. Conduct
  - n/a
- 10. Performance
  - -p.88 S(3) contrary to public interest
  - Stage II
  - S.4(a) Primary Consequences, i.e. decrease barriers to entry
  - Stage III
  - S.4(b) Secondary Consequences i.e. real economies
  - Stage IV Remedy
- 11. Economies Defence
  - Stage II balancing
    "effectively offset", p. 89
- 12. Failing Company Defence
  - -p.87, S.4(c)(ii) - not automatic
    - also, structural rationalization exemption
- 13. Relevant Market
  - -p.79,85 Pertinent Market
    11 Criteria
    See PSW, p. 87, p. 266
- 14. International Mergers
  - -p.68,80,105-112 - reject FIRA
  - -"beneficial impact on competition" p.339
  - -same rules as for domestic

IV. PRE-MERGER REQUIREMENTS
- 15. Registration
  - -S.2,p.124 Within 1 year DIR learns of merger, he may apply to Board
  - -p.337 Advance Ruling
    (a) 30 days to inquiry
    (b) 60 days to Board or deemed approved
    (c) Integrated with FIRA
- 16. Pre-Clearance
  - n/a
- 17. Pre-Notification
  - n/a

V. REMEDIES
- 18. Fines
  - n/a
- 19. Prison
  - n/a
- 20. Patents
  - -p.89 (a) alter the reaction pattern of industry
    (b) enjoin
- 21. Tariffs/Quotas
  - -p.89
- 22. Orders: Divest, Dissolve, Prohibit
  - -p.89
  - -p.301 - dissolution not to be set aside by Court
  - -p.302 - Court can review divestiture order
- 23. Conditional Orders
  - -p.303 - Interim injunction 90 days
- 24. Final Orders
  - n/a
- 25. Damages
  - To Courts
- 26. Publications
- 27. Interim Injunctions
  - -p.302 - primo facie case
    - reviewable by Court
    - separate & apart

VI. APPEALS
- 28. Appeals
  - -p.307 - no appeal on remedies
    - exceptions:
      (a) divestiture
      (b) Interim Injunction
  - -p.311 - Federal Court Act S.28

VII. MISCELLANEOUS
- 29. Intent
  - n/a
- 30. Class Actions
  - -p.324-326 recommend with caveats
- 31. Provincial Coordination
  - n/a

TABLE 6

1977 Bill C-42

I. ADJUDICATION

1. Court v. Tribunal
   - -S.5(1) Competition Policy Advocate
   - -S.16(1) Competition Board
     - quasi-judicial
     - near applications from C.P.A.
     - *not* report to Minister
     - *not* intermediate hearings
2. Powers of Tribunal/RTPC/DIR
   - -S.47 C.P.A. conducts Inquiry
     - (a) on own initiative
     - (b) request of Minister *not* on request of the Board
   - -S.47(5) Second Inquiry
   - -S.17(1) Hearing Officer - presides over hearing evidence during Inquiry
   - -S.31.91(1) Preliminary Hearing
3. Civil v. Criminal
   - Civil, S.33 repeated
   - -S.31.71 is reviewable

II. INVESTIGATION

4. Search and Seizure
   - -S.10 includes "thing"
   - -S.10.1 solicitor-client privilege

III. MERGER TEST

5. Horizontal
   - -S.31.71(1) defines merger to include all three types
6. Vertical
   - S.37.1(4)(j) market foreclosure
7. Conglomerate
   - n/a
8. Structure
   - -S.31.71(4) (a) substitutes
     - (b) imports
     - (c) trend to conc. Etc.
   - -S.31.71(2) market share for HORZ mergers greater than 20%
9. Conduct
   - -S.31.71(4)(g) history of anti-competitive behaviors
10. Performance
    - -S.31.71 lessens actual or potential competition substantially -AND- for HORZ mergers, results in market share greater than 20%
11. Economies Defence
    - -S.31.71(5) satisfied, *high* probability, substantial gains in efficiency, by real resource savings, not attainable otherwise
    - -S.31.71(7) virtual monopoly; Board shall make order
12. Failing Company Defence
    - -S.31.71(4)(n) likelihood party about to fail
13. Relevant Market
    - -S.31.71(2) no definition of HORZ merger greater than 20% of *any* "market"
    - -S.31.71(12) "affiliated"
14. International Mergers
    - -S.31.71(9)(10)(11) FIRA must notify CPA of all proposed mergers decision of FIRA does *not* affect CPA

IV. PRE-MERGER REQUIREMENTS

15. Registration
    - omitted
16. Pre-Clearance
    - n/a
17. Pre-Notification
    - omitted

V. REMEDIES

18. Fines
    - n/a
19. Prison
    - n/a
20. Patents
    - -S.31.71(6)
21. Tariffs/Quotas
    - -S.31.71(6)
22. Orders: Divest, Dissolve, Prohibit
    - -S.30(1) prohibit continuation of offence or any act directed toward
    - -S.30(2) dismiss prosecution and makr order require consent of A.G. and accused
23. Conditional Orders
    - -S.31.71(7) If Board can order:
      - (a) reduce tariffs
      - (b) irreversible act
      - the conditional
24. Final Orders
    - -S.31.71(3) Dissolve, Divest, Prohibit
    - -S.31.71(6) irreversible change
25. Damages
    - -S.31.1(1.1)any other remedy in addition
26. Publications
    - n/a
27. Interim Injunctions
    - -S.29.1(1) - appears
      - *prima facie* case
      - serious injury to competition or another's business
      - expedite proceedings

VI. APPEALS

28. Appeals
    - -S.31.91(2) no appeal of Prelim.
    - -S.28 FCA general appeal

VII. MISCELLANEOUS

29. Intent
    - -S.37.1(4)(l) intent to reduce competition
30. Class Actions
    - Part VI
    - -S.39.11 Class Action
      - *prima facie* case, S.31.1
      - no superior method available
    - -S.39.14 Substitute Action
31. Provincial Coordination
    - n/a

- Separate secti 'art IV.1

TABLE 7

1977 Bill C-13

I. ADJUDICATION
1. Court v. Tribunal
    n/a
2. Powers of Tribunal/RTPC/DIR
    -S.31.91(1) Preliminary Hearing "ex parte" to prove "prima facie"
    case by C.P.A. to Board deleted
    -D S.27.2 Interpretitive Opinions
3. Civil v. Criminal
    -S.16, 16.5 Criminal to civil

II. INVESTIGATION
4. Search and Seizure
    as in C-42

III. MERGER TEST
5. Horizontal
    -S.31.71(1) definition includes joint venture
6. Vertical
    -S.31.71(1) definition includes joint venture
7. Conglomerate
    n/a
8. Structure
    -S.31.71(4) includes general factor clause
9. Conduct
    n/a
10. Performance
    n/a
11. Economies Defence
    -S.31.71(5) must hear parties, clear probability, omit other ways
12. Failing Company Defence
    n/a
13. Relevant Market
    n/a
14. International Mergers
    -S.31.71(13)-(17) clarifies relationship with FIRA

IV. PRE-MERGER REQUIREMENTS
15. Registration
    n/a
16. Pre-Clearance
    n/a
17. Pre-Notification
    -S.31.71(19)(20) Advance Ruling
    - CPA issues certificate which precludes
    application for order
    - where CPA 'satisfied'
    - D 'identical' to C-91
    -S.31.71(21)(22) Notification
    - CPA precuded from order after 6 (up to 12) months

V. REMEDIES
18. Fines
    n/a
19. Prison
    n/a
20. Patents
    n/a
21. Tariffs/Quotas
    n/a
22. Orders: Divest, Dissolve, Prohibit
    -S.31.79.1 Consent Orders
23. Conditional Orders
    n/a
24. Final Orders
    n/a
25. Damages
    -S.31.1(1.1) retained
26. Publications
    n/a
27. Interim Injunctions
    -S.29.1(1) Adds requirements
    (a) of hearing all parties

    (b) general principles re civil injunctions

VI. APPEALS
28. Appeals
    -S.31.91(1) appeal to Cabinet in addition
    -no appeal to Courts

VII. MISCELLANEOUS
29. Intent
    n/a
30. Class Actions
    Class actions retained
    Deleted substitute actions
31. Provincial Coordination
    n/a

TABLE 8

1978 Report of the Royal Commission on Corporate Concentration

I. ADJUDICATION

1. Court v. Tribunal
   -p.102 Act should have "sunset clause"
2. Powers of Tribunal/RTPC/DIR
   n/a
3. Civil v. Criminal
   n/a

II. INVESTIGATION

4. Search and Seizure
   n/a

III. MERGER TEST

5. Horizontal
   -p.166 No Pre-Merger Test Recommended. But, reviewable if:
   (a) 50% post-merger market share, plus
   (b) $50M assets/shares
6. Vertical
   -p.166 No Pre-Merger Test Recommended. But, reviewable if:
   (a) one party has pre-merger 50% market share, plus
   (b) $50M assets/shares
7. Conglomerate
   -p.166 No Pre-Merger Test Recommended. But, reviewable if:
   (a) as HORZ or VERT
   -OR-
   (b) PURE CONG, by Cabinet

   Ch.15
   -p.126 diversification into "related" business improved performance
   -p.133 no reciprocity
   -p.129 no cross-subsidization
8. Structure
   n/a
9. Conduct
   -p.166 recommends conduct post-merger test
10. Performance
    n/a
11. Economies Defence
    Ch.13,p.43,p.53 - product more important than plant economies
    - firm economies most important
    -p.12 - policy conundrum: economies v. market power
    - tariffs & foreign ownership
12. Failing Company Defence
    n/a
13. Relevant Market
    n/a
14. International Mergers
    n/a

IV. PRE-MERGER REQUIREMENTS

15. Registration
    omitted
16. Pre-Clearance
    n/a
17. Pre-Notification
    -p.155 Mergers do not create economies
    -p.158 Mergers do not decrease competition; therefore recommend no review process or p.161,162,165

V. REMEDIES

18. Fines
    n/a
19. Prison
    n/a
20. Patents
    n/a
21. Tariffs/Quotas
    -p.67 (a) tariffs
    (b) foreign ownership are more important source of economies
    - selective tariff reduction
22. Orders: Divest, Dissolve, Prohibit
    -p.165,166 agree with Consent Orders
    BUT, need safeguards. Board should
    (a) review
    (b) approve
    (c) publish
23. Conditional Orders
    n/a
24. Final Orders
    n/a
25. Damages
    n/a
26. Publications
    n/a
27. Interim Injunctions
    -p.160 Act should deal with proven anticompetitive conduct; therefore no interim injunctions

VI. APPEALS

28. Appeals
    -p.163 jurisdiction and procedure to Courts
    no appeal of substance
    no appeal to Cabinet

VII. MISCELLANEOUS

29. Intent
    n/a
30. Class Actions
    n/a
31. Provincial Coordination
    n/a

TABLE 9

1981 Proposals

I. ADJUDICATION
- 1. Court v. Tribunal
  - Courts (n.7, 18)
  - Federal Court v. Prov. Courts (n.9)
- 2. Powers of Tribunal/RTPC/DIR
  - n/a
- 3. Civil v. Criminal
  - Civil (n.15)

II. INVESTIGATION
- 4. Search and Seizure
  - n/a

III. MERGER TEST
- 5. Horizontal
  - n/a
- 6. Vertical
  - degree of market foreclosure (n.19)
- 7. Conglomerate
  - n/a
- 8. Structure
  - PRESUMPTIVE THRESHOLD
  - - "deeming provision" if market share over % deemed to lessen competition significantly (n.18)
  - - still allow merger, if conditional order available (n.18)
- 9. Conduct
  - n/a
- 10. Performance
  - - lessens competition "significantly" (n.18)
  - - no public detriment
- 11. Economies Defence
  - NONE (n.16, 18)
- 12. Failing Company Defence
  - n/a
- 13. Relevant Market
  - n/a
- 14. International Mergers
  - - follow C-13 (n.22)
  - - FIRA - deals with foreign investment
  - - DIR - deals with competition policy

IV. PRE-MERGER REQUIREMENTS
- 15. Registration
  - n/a
- 16. Pre-Clearance
  - n/a
- 17. Pre-Notification
  - REPORTING THRESHOLD
  - - "Extremely Large" mergers must pre-notify
  - - on HORZ or VERT
  - - 60 day to contest, or DIR barred (n.21)
  - - n.23, question 5
  - - first pre-notification

V. REMEDIES
- 18. Fines
  - n/a
- 19. Prison
  - n/a
- 20. Patents
  - available (n.18)
- 21. Tariffs/Quotas
  - available (n.18)
- 22. Orders: Divest, Dissolve, Prohibit
  - available (n.18)
- 23. Conditional Orders
  - available (n.18) to avoid "dominant position"
- 24. Final Orders
  - n/a
- 25. Damages
  - n/a
- 26. Publications
  - n/a
- 27. Interim Injunctions
  - n/a

VI. APPEALS
- 28. Appeals
  - n/a

VII. MISCELLANEOUS
- 29. Intent
  - n/a
- 30. Class Actions
  - n/a
- 31. Provincial Coordination
  - n/a

TABLE 10

1984 Bill C-29

I. ADJUDICATION
- 1. Court v. Tribunal
  - -S.31.72 Court-upon application of DIR
- 2. Powers of Tribunal/RTPC/DIR
  - n/a
- 3. Civil v. Criminal
  - Civil

II. INVESTIGATION
- 4. Search and Seizure
  - -DIR to inform party of progress of inquiry
  - -no search warrant
  - -solicitor-client privilege (s.10.2)

III. MERGER TEST
- 5. Horizontal
  - n/a
- 6. Vertical
  - -S.31.74(1)(h) foreclosure
- 7. Conglomerate
  - omitted
- 8. Structure
  - n/a
- 9. Conduct
  - -S.31.74(1)(c)
- 10. Performance
  - -S.31.71 Definition
    - establish
    - amalgamation
  - -S.31.72 TEST "lessens competition significantly"
  - -S.31.74(2) - significant = not insubstantial
  - -S.31.74(1) - Factors to be considered
    - any relevant factor
- 11. Economies Defence
  - -S.31.73 - "substantial real net savings of resources"
    - not attainable otherwise
    - Court shall not make order if:
      - "substantial real net savings of resources"
      - not attainable otherwise
- 12. Failing Company Defence
  - -S.31.74(1)(a) likelihood
- 13. Relevant Market
  - n/a
- 14. International Mergers
  - n/a

IV. PRE-MERGER REQUIREMENTS
- 15. Registration
  - n/a
- 16. Pre-Clearance
  - n/a
- 17. Pre-Notification
  - ADVANCE RULING
  - -S.31.791 - DIR satisfied not sufficient grounds under S.31.72
    - bars DIR if merger complete in 1 year
    - identical to C-91 except: - apply to court
      - different test
  - -precursor to C-91
  - -addresses RRCCC, 1981 Proposals
  - PRE-NOTIFICATION
  - -S.31.81 - acquisition
  - -S.31.84 - amalgamation
  - NOTIFIABLE TRANSACTION
  - -S.31.8 - Operating business assets/sales over $10M, and
  - -S.31.86 - $500M assets-post merger
  - ACQUIRED FIRM
  - -S.31.82 - 20% shares
  - -S.31.83 - $35M
  - -S.31.891 - short form
  - -S.31.892 - long form
  - -S.31.89(2) waiting period
    - 21 days for interim
    - 21 days for Court determination

V. REMEDIES
- 18. Fines
  - n/a
- 19. Prison
  - n/a
- 20. Patents
  - n/a
- 21. Tariffs/Quotas
  - -S.31.77(1) (a) may rescind or vary order if tariffs reduced
    - (b) any other measure
- 22. Orders: Divest, Dissolve, Prohibit
  - -S.31.72 (e) completed merger
    - (f) proposed merger
- 23. Conditional Orders
  - -S.31.77
- 24. Final Orders
  - n/a
- 25. Damages
  - n/a
- 26. Publications
  - n/a
- 27. Interim Injunctions
  - -S.31.78 - no S.31.72 order
  - (no applic.)-"reasonably likely to lessen competition significantly"
    - PLUS
    - action difficult to reverse
    - OR, failure to pre-notify S.31.8
  - -S.31.91 (where application made)

VI. APPEALS
- 28. Appeals
  - -S.31.75 3 year limitation period

VII. MISCELLANEOUS
- 29. Intent
  - -S.31.74(1)(g)
- 30. Class Actions
  - n/a
- 31. Provincial Coordination
  - n/a

TABLE 11

1985 Proposals

I. ADJUDICATION
- 1. Court v. Tribunal
  - n.10 Tribunal
- 2. Powers of Tribunal/RTPC/DIR
  - n/a
- 3. Civil v. Criminal
  - n.4 civil

II. INVESTIGATION
- 4. Search and Seizure
  - n.23 search orders to be obtained from Judge (not RTPC) to separate investigatory -AND- adjudicative roles

III. MERGER TEST
- 5. Horizontal
  - n/a
- 6. Vertical
  - n/a
- 7. Conglomerate
  - n/a
- 8. Structure
  - n/a
- 9. Conduct
  - n/a
- 10. Performance
  - n.35 lessen competition substantially
  - n.45 joint ventures not exempted
- 11. Economies Defence
  - n.37 weigh the costs & benefits
  - n.39 not absolute defence
  - n.40 not "pass on to consumer" defence
- 12. Failing Company Defence
  - n/a
- 13. Relevant Market
  - n/a
- 14. International Mergers
  - n.31 enhance international competitiveness opportunity of foreigns to compete domestically hampered

IV. PRE-MERGER REQUIREMENTS
- 15. Registration
  - n/a
- 16. Pre-Clearance
  - n/a
- 17. Pre-Notification
  - n.49 too complex, "operating business" irrelevant
  - n.51 eliminate short form
  - n.52 extend waiting period
  - n.53 Info requirements should be in Regulations

V. REMEDIES
- 18. Fines
  - n/a
- 19. Prison
  - n/a
- 20. Patents
  - n/a
- 21. Tariffs/Quotas
  - -S.65(1)(iv)
- 22. Orders: Divest, Dissolve, Prohibit
  - n/a
- 23. Conditional Orders
  - n/a
- 24. Final Orders
  - n/a
- 25. Damages
  - n/a
- 26. Publications
  - n/a
- 27. Interim Injunctions
  - n/a

VI. APPEALS
- 28. Appeals
  - n.11 Cabinet override

VII. MISCELLANEOUS
- 29. Intent
  - n/a
- 30. Class Actions
  - n/a
- 31. Provincial Coordination
  - n/a

TABLE 12

1985 McDonald Report

I. ADJUDICATION
  1. Court v. Tribunal
    -p. 225 Tribunal
  2. Powers of Tribunal/RTPC/DIR
    n/a
  3. Civil v. Criminal
    n/a

II. INVESTIGATION
  4. Search and Seizure
    n/a

III. MERGER TEST
  5. Horizontal
    -p.222 lessen competition significantly
  6. Vertical
    -p.227 no test available
  7. Conglomerate
    -p.222 should not be subject to review
    -p.224 dealt with on individual basis
  8. Structure
    n/a
  9. Conduct
    n/a
  10. Performance
    -p.220 In free trade or deregulated economy do not need merger prohibition
    -p.222 lessen competition significantly
  11. Economies Defence
    -p.218 balancing, product specific economies
  12. Failing Company Defence
    n/a
  13. Relevant Market
    n/a
  14. International Mergers
    -p.220,216 promote comp through
      (a) free trade
      (b) deregulation

IV. PRE-MERGER REQUIREMENTS
  15. Registration
    n/a
  16. Pre-Clearance
    n/a
  17. Pre-Notification
    -p.227 require extensive information

V. REMEDIES
  18. Fines
    n/a
  19. Prison
    n/a
  20. Patents
    n/a
  21. Tariffs/Quotas
    n/a
  22. Orders: Divest, Dissolve, Prohibit
    n/a
  23. Conditional Orders
    n/a
  24. Final Orders
    n/a
  25. Damages
    n/a
  26. Publications
    n/a
  27. Interim Injunctions
    n/a

VI. APPEALS
  28. Appeals
    n/a

VII. MISCELLANEOUS
  29. Intent
    n/a
  30. Class Actions
    n/a
  31. Provincial Coordination
    n/a

TABLE 13

1985 Bill C-91

I. ADJUDICATION
1. Court v. Tribunal
   Part I Competition Tribunal Act
   -S.(3) 4 judges, 8 laypeople
   -S.64(1) Tribunal to hear Competition Act Part VII applications
2. Powers of Tribunal/RTPC/DIR
   -S.8 DIR Investigate Part VII
   -S.8(2) DIR must inform party of inquiry progress
   RTPC terminated
   Solely adjudicative (repeal S.47)
   -S.64(1) tribunal to hear mergers
3. Civil v. Criminal
   civil

II. INVESTIGATION
4. Search and Seizure
   -S.13 reasonable and probable grounds - warrant from judge
   -S.15 DIR to take before judge or report - subpoena & produce documents

III. MERGER TEST
5. Horizontal
   -S.63 "control on significant interest in", exempts joint ventures (also, S.67)
   -4 methods of merger
6. Vertical
   n/a
7. Conglomerate
   n/a
8. Structure
   n/a
9. Conduct
   n/a

10. Performance
   -S.64(1) likelihood to lessen competition substantially
   -S.64(2) do not evaluate effect solely on market share
   -S.65(1) (v) substantial competition remaining
   -S.65 Factors
   -S.66,67,68 Exemptions
11. Economies Defence
   -S.68(1) likelihood
   (a) efficiencies be greater than, and will offset, the effects, of merger on competition
   (b) and, gains unlikely if merger disallowed
   (c) X and M competition
   (d) not just redistribution
12. Failing Company Defence
   -S.65(1)(ii)
13. Relevant Market
   -S.65(1)(c) available substitutes
14. International Mergers
   -S.65(1)(i) foreign competitors provide effective competition

IV. PRE-MERGER REQUIREMENTS
15. Registration
   n/a
16. Pre-Clearance
   n/a
17. Pre-Notification
   -S.74 PRE-CLEARANCE
   - DIR satisfied would not have sufficient amounts
   - 1 year to complete merger
   -S.82 PRE-NOTIFICATION
   -S.80 Notifiable Transaction "Operating Business", employees report
   -S.81 Assets/Revenue greater than $400M
   D-S.82(1) Parties Threshold
   -S.82(2) Asset Transaction Threshold
   -S.82(3) Share Transaction Threshold
   -S.82(3) Acquisition
   -S.82(4) Amalgamation
   -S.82(5) Combination
   -S.83 Exemptions
   D-S.84 Joint Ventures
   -S.85 General exemptions
   -S.86 Notify & Inform
   -S.93 Short Form
   -S.94 Long Form
   -S.95 Waiting Period

V. REMEDIES
18. Fines
   n/a
19. Prison
   n/a
20. Patents
   n/a
21. Tariffs/Quotas
   -S.28 Cabinet satisfied tariffs causing lessening of comp. substantially
   -S.71 conditional S.64 order
22. Orders: Divest, Dissolve, Prohibit
   -S.30(1),(2) delete merger dissolution reference
23. Conditional Orders
   INCOMPLETE
   -S.64(1)(f) consent, conditional, hold separate
   COMPLETE
   -S.64(1)(e) dissolution
26. Publications
   n/a
27. Interim Injunctions
   -S.72 Pre-Application
   (a) "prima facie" case merger reasonably likely to lessen comp. substantially, and
   (b) no order would impair future remedy
   (c) 21 day no-extension maximum (10 days, 'ex parte')
   -S.76 Post-Application
   (a) balance of convenience
   -S.11 one judicial member to hear

VI. APPEALS
28. Appeals
   -S.13 Appeal to Federal Court of Appeal - all matters
   -no cabinet S.13(2) appeal of fact, with leave

VII. MISCELLANEOUS
29. Intent
   n/a
30. Class Actions
   n/a
31. Provincial Coordination
   n/a

APPENDIX B

SYNOPSIS OF THE INFLUENCIAL CANADIAN CASES

					LESSENING COMPETITION				DETRIMENT				
CASE	YEAR COURT JUDGE	CHARGE	VERDICT	UNDUENESS	NO PRESUMPTION	INFERENCE	REBUTTABLE PRESUMPTION	IRREBUTTABLE PRESUMPTION	NO PRESUMPTION	INFERENCE	REBUTTABLE PRESUMPTION	IRREBUTTABLE PRESUMPTION	'PER SE' RULE
R v. Elliott	1905 Ont. C.A. Osler, J.	conspiracy	dismissed	wrongly improperly excessively inordinately	Yes Implied								
Weldman v. Shragge	1912 SCC Anglin, J.	conspiracy	dismissed	improper inordinate excessive oppressive (p.42 S.R.R.)	Yes Implied								
Adelaide	1913 P.C. Lord Parker (Australia)	conspiracy	dismissed		Yes: wrongful intent must be proved (p.781 A.C.)								
Stinson-Reeb	1929 S.C.C. Mignault, J.	conspiracy	dismissed	1. applied Weldman	Yes								
Alexander	1932 Ont. S.C. Raney, J.	conspiracy											
Container Materials	1942 S.C.C. Duff, C.J.	conspiracy	conviction	1. a matter of fact 2. applied Stinsun-Reeb	Yes								
Eddy Match	1951 Que. C.A.	monopoly	conviction	Complete Control							Yes: but not rebutted in this case (p.20 C.C.C.)		
Northern Electric	1955 Ont. H.C. McRuer, J.	conspiracy		virtual monopoly not necessary condition									
Morrey	1956 B.C.C.A. Smith, J.A.	pre-1960 monopoly/merger	acquittal						Yes 1. must prove detriment 2. proof of lessening comp. insufficient				
Howard Smith	1959 S.C.C. Cartwright, J. Kellock, J.	conspiracy	conviction	"virtually unaffected by comp." test	Yes							Yes: conclusively presumed from undue less. of comp.	

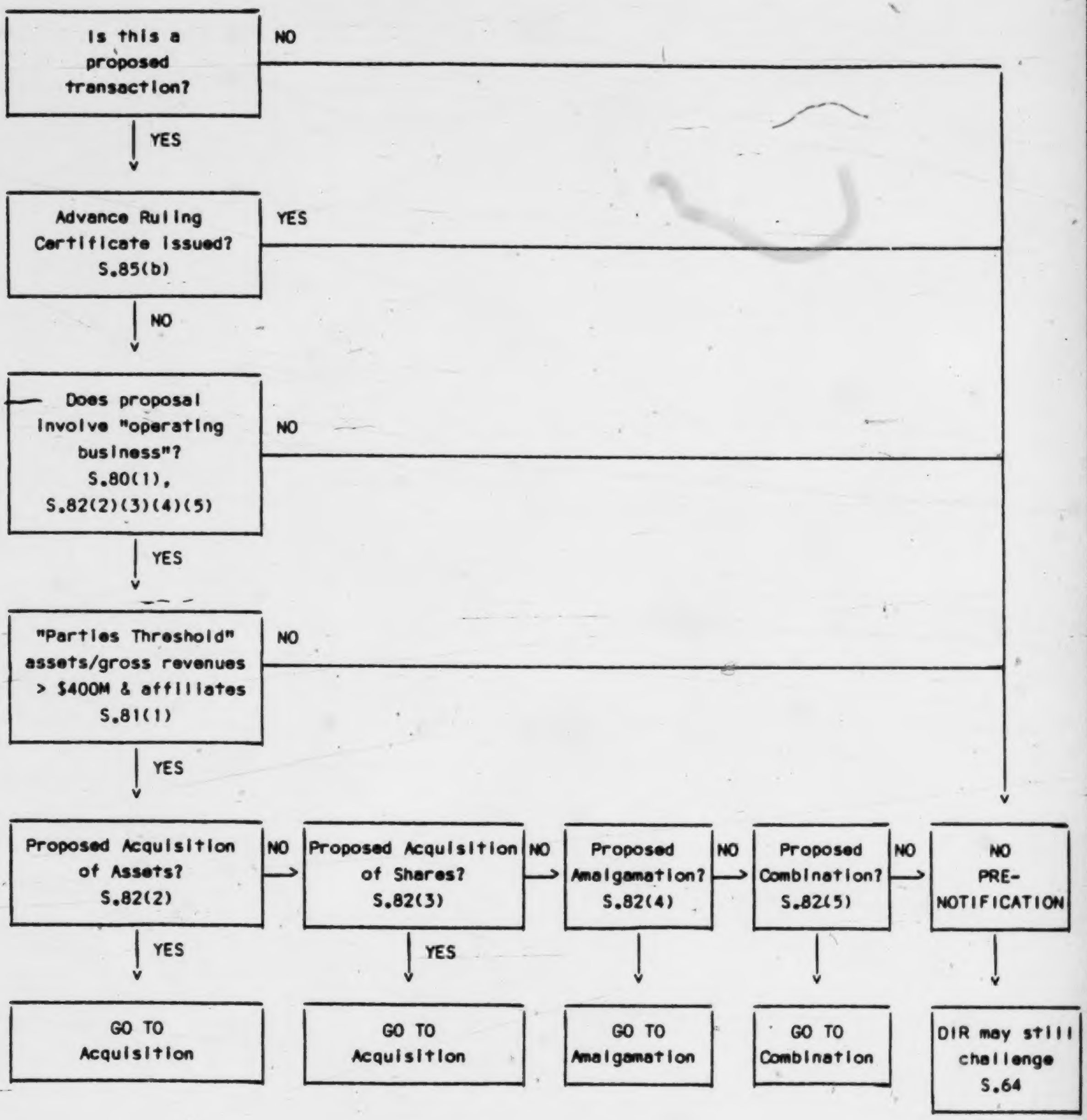
CASE	YEAR COURT JUDGE	CHARGE	VERDICT	UNDUENESS	LESSENING COMPETITION NO PRESUMPTION	LESSENING COMPETITION INFERENCE	LESSENING COMPETITION REBUTTABLE PRESUMPTION	LESSENING COMPETITION IRREBUTTABLE PRESUMPTION	DETRIMENT NO PRESUMPTION	DETRIMENT INFERENCE	DETRIMENT REBUTTABLE PRESUMPTION	DETRIMENT IRREBUTTABLE PRESUMPTION	'PER SE' RULE
Canadian Breweries	1960 Ont. H.C. McRuer, J.	pre-1960 merger	acquittal	Virtual Monopoly necessary condition	Yes no comp. remaining				not decided				
B.C. Sugar	1960 Man. Q.B. Williams, C.J.Q.B.	pre-1960 merger	acquittal	Virtual Monopoly necessary condition					1. causation - by merger 2. detriment - prove (a) power (b) exorbitant Prices or Profits (c) virtual stifling of comp. 3. "Compound Test"-operate unduly to Detriment				
Cdn. Coat & Apron	1967	conspiracy										Yes	Yes -vague -probably synonymous with irrebutable presumption
Irving Trial	1974 NBSC Robichaud, J.	pre-1960 Monopoly Merger post-1960 Monopoly Merger	conviction	1. any lessening of competition ⟶ 'per se' rule 2. or, undue lessening								YES: As a result of any lessening of competition	YES
Irving C.A.	1975 N.B.S.C.(A.D.) Limmerick, J.A.		acquittal						Yes: (p.488 C.C.C.)		Possibly: Strong obiter that inference is rebuttable		
Irving S.C.C.	1976 S.C.C. Laskin, C.J.C.		acquittal			Complete Control may lead to no presumption -OR- a rebuttable presumption of lessening competition (p.12 C.C.C.)			Yes: (p.12 C.C.C.)				

APPENDIX C

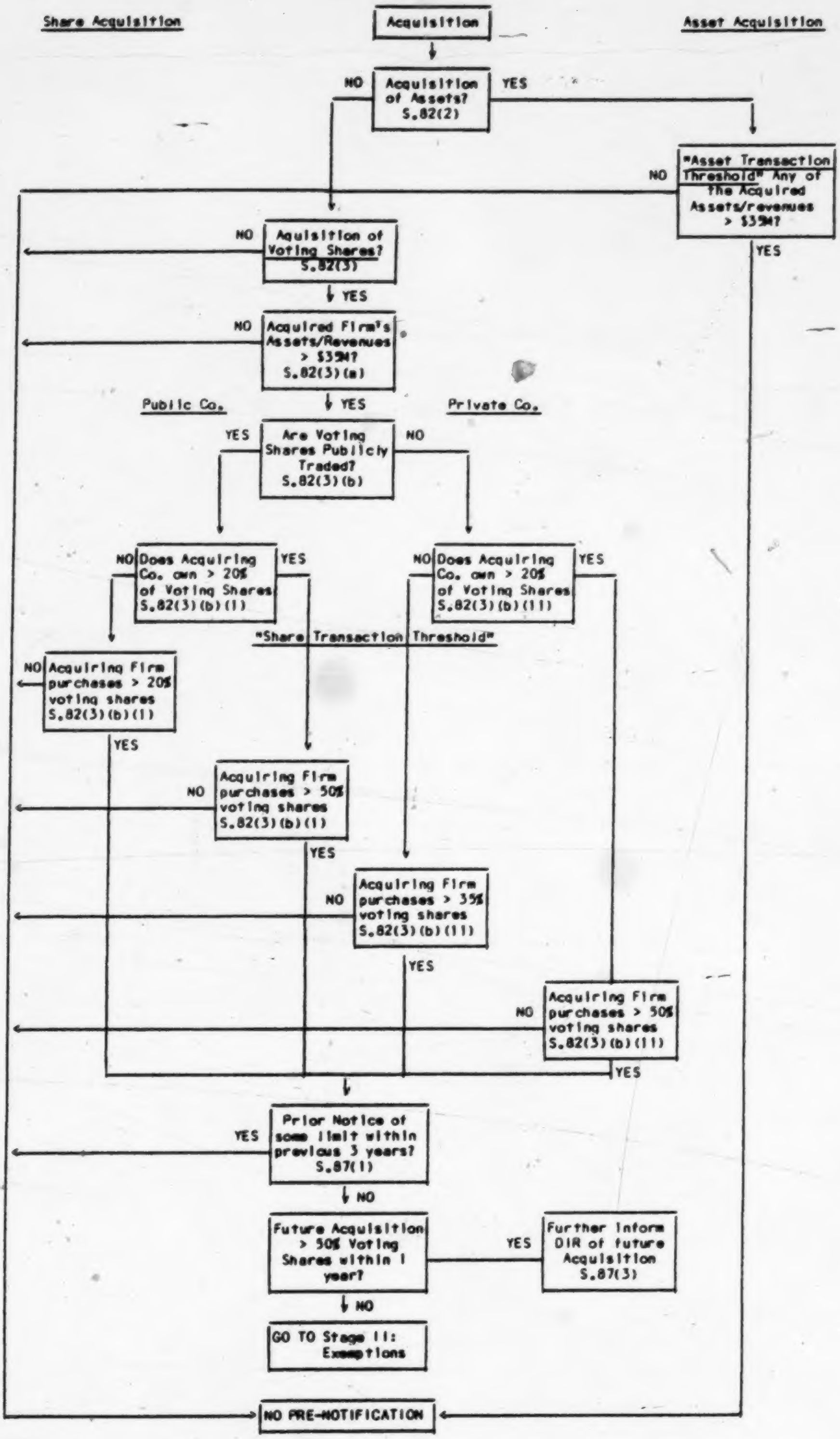
FLOWCHART OF NOTIFIABLE TRANSACTIONS

STAGE I

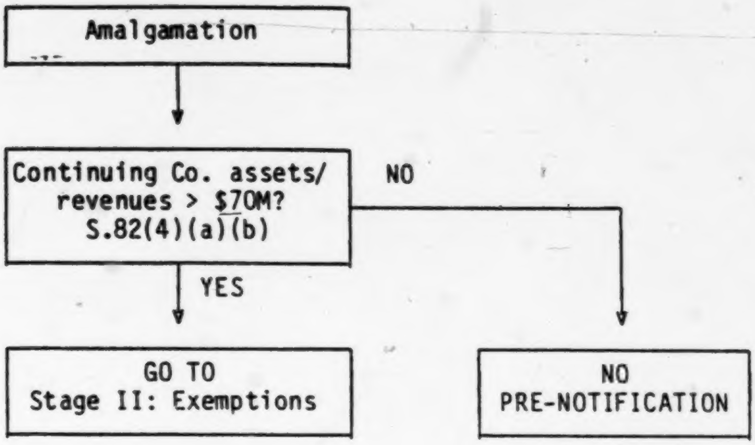
Notifiable Transactions


Is this a proposed transaction?
NO
YES
Advance Ruling Certificate issued? S.85(b)
YES
NO
Does proposal involve "operating business"? S.80(1), S.82(2)(3)(4)(5)
NO
YES
"Parties Threshold" assets/gross revenues > $400M & affiliates S.81(1)
NO
YES
Proposed Acquisition of Assets? S.82(2)
NO
Proposed Acquisition of Shares? S.82(3)
NO
Proposed Amalgamation? S.82(4)
NO
Proposed Combination? S.82(5)
NO
NO PRE-NOTIFICATION
YES
YES
GO TO Acquisition
GO TO Acquisition
GO TO Amalgamation
GO TO Combination
DIR may still challenge S.64

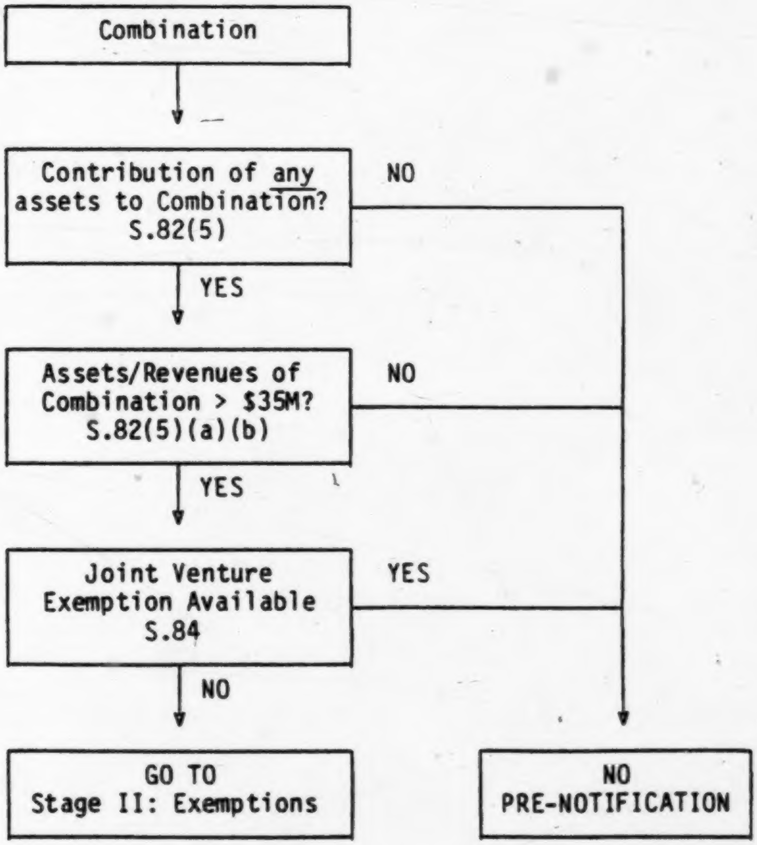
Proposed Acquisitions


Share Acquisition
Acquisition
Asset Acquisition
NO
Acquisition of Assets? S.82(2)
YES
"Asset Transaction Threshold" Any of The Acquired Assets/revenues > $35M?
NO
YES
NO
Aquisition of Voting Shares? S.82(3)
YES
NO
Acquired Firm's Assets/Revenues > $35M? S.82(3)(a)
YES
Public Co.
Private Co.
YES
Are Voting Shares Publicly Traded? S.82(3)(b)
NO
NO
Does Acquiring Co. own > 20% of Voting Shares S.82(3)(b)(i)
YES
NO
Does Acquiring Co. own > 20% of Voting Shares S.82(3)(b)(ii)
YES
"Share Transaction Threshold"
NO
Acquiring Firm purchases > 20% voting shares S.82(3)(b)(i)
YES
NO
Acquiring Firm purchases > 50% voting shares S.82(3)(b)(i)
YES
NO
Acquiring Firm purchases > 35% voting shares S.82(3)(b)(ii)
YES
NO
Acquiring Firm purchases > 50% voting shares S.82(3)(b)(ii)
YES
YES
Prior Notice of some limit within previous 3 years? S.87(1)
NO
Future Acquisition > 50% Voting Shares within 1 year?
YES
Further inform DIR of future Acquisition S.87(3)
NO
GO TO Stage II: Exemptions
NO PRE-NOTIFICATION

Proposed Amalgamation

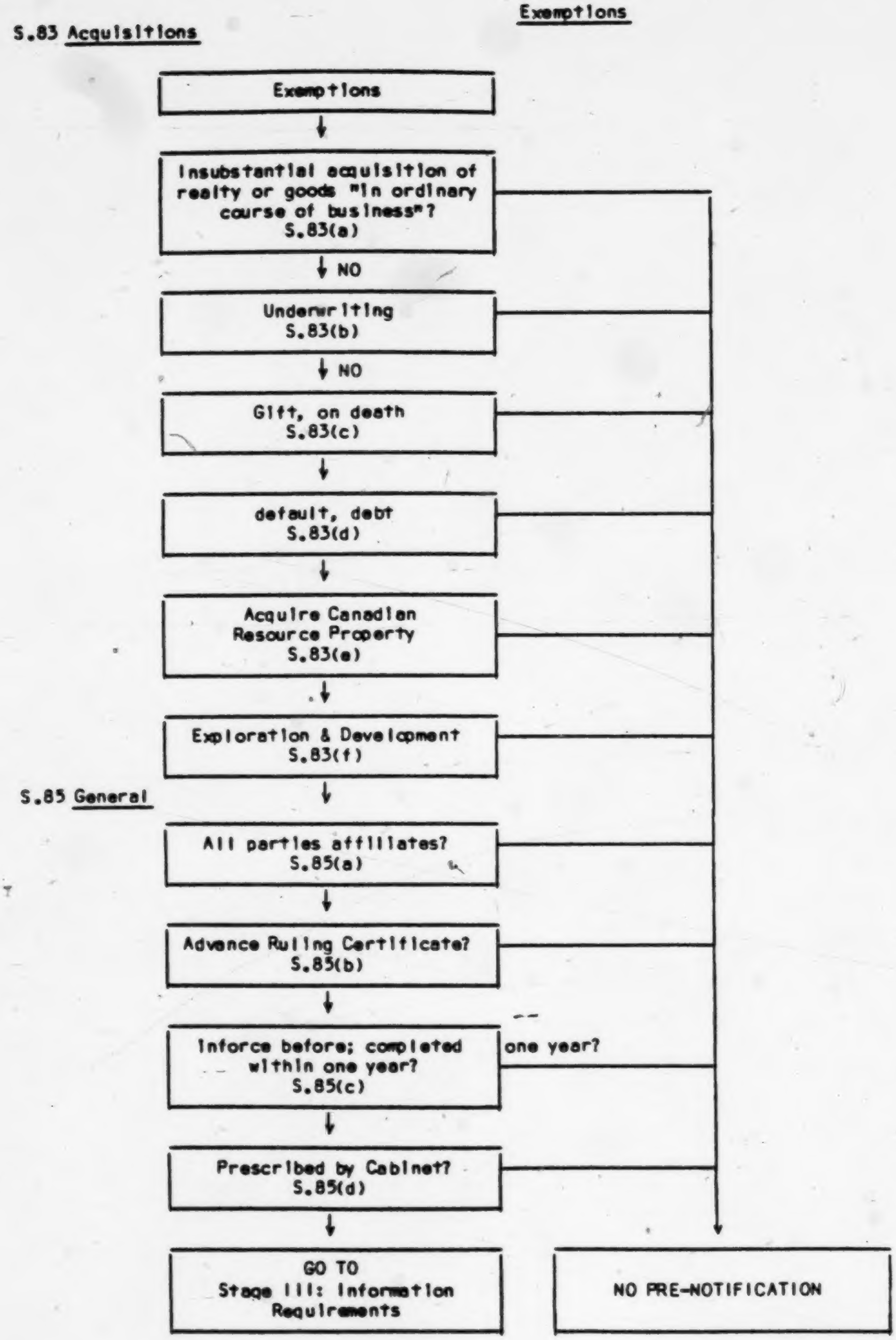

Amalgamation
Continuing Co. assets/ revenues > $70M? S.82(4)(a)(b)
NO
YES
GO TO Stage II: Exemptions
NO PRE-NOTIFICATION

Proposed Combination


Combination
Contribution of any assets to Combination? S.82(5)
NO
YES
Assets/Revenues of Combination > $35M? S.82(5)(a)(b)
NO
YES
Joint Venture Exemption Available S.84
YES
NO
GO TO Stage II: Exemptions
NO PRE-NOTIFICATION

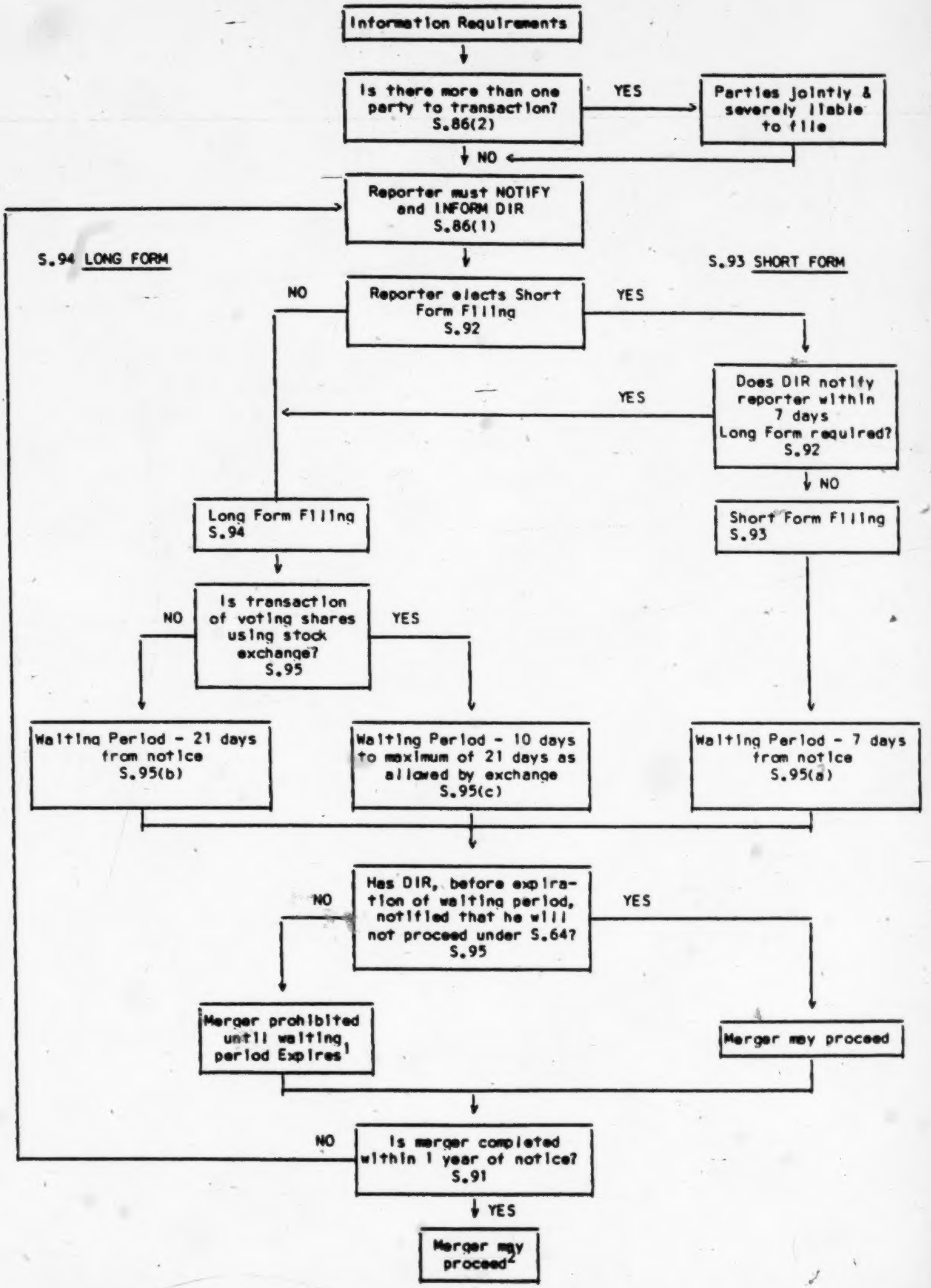
Stage II

Exemptions


S.83 Acquisitions
Exemptions
Insubstantial acquisition of realty or goods "in ordinary course of business"? S.83(a)
NO
Underwriting S.83(b)
NO
Gift, on death S.83(c)
default, debt S.83(d)
Acquire Canadian Resource Property S.83(e)
Exploration & Development S.83(f)
S.85 General
All parties affiliates? S.85(a)
Advance Ruling Certificate? S.85(b)
Inforce before; completed within one year? S.85(c)
one year?
Prescribed by Cabinet? S.85(d)
GO TO Stage III: Information Requirements
NO PRE-NOTIFICATION

Stage III

Information Requirements


Information Requirements
Is there more than one party to transaction? S.86(2)
YES
Parties jointly & severely liable to file
NO
Reporter must NOTIFY and INFORM DIR S.86(1)
S.94 LONG FORM
S.93 SHORT FORM
NO
Reporter elects Short Form Filing S.92
YES
YES
Does DIR notify reporter within 7 days Long Form required? S.92
NO
Long Form Filing S.94
Short Form Filing S.93
NO
Is transaction of voting shares using stock exchange? S.95
YES
Waiting Period - 21 days from notice S.95(b)
Waiting Period - 10 days to maximum of 21 days as allowed by exchange S.95(c)
Waiting Period - 7 days from notice S.95(a)
NO
Has DIR, before expiration of waiting period, notified that he will not proceed under S.64? S.95
YES
Merger prohibited until waiting period Expires[1]
Merger may proceed
NO
Is merger completed within 1 year of notice? S.91
YES
Merger may proceed[2]

---

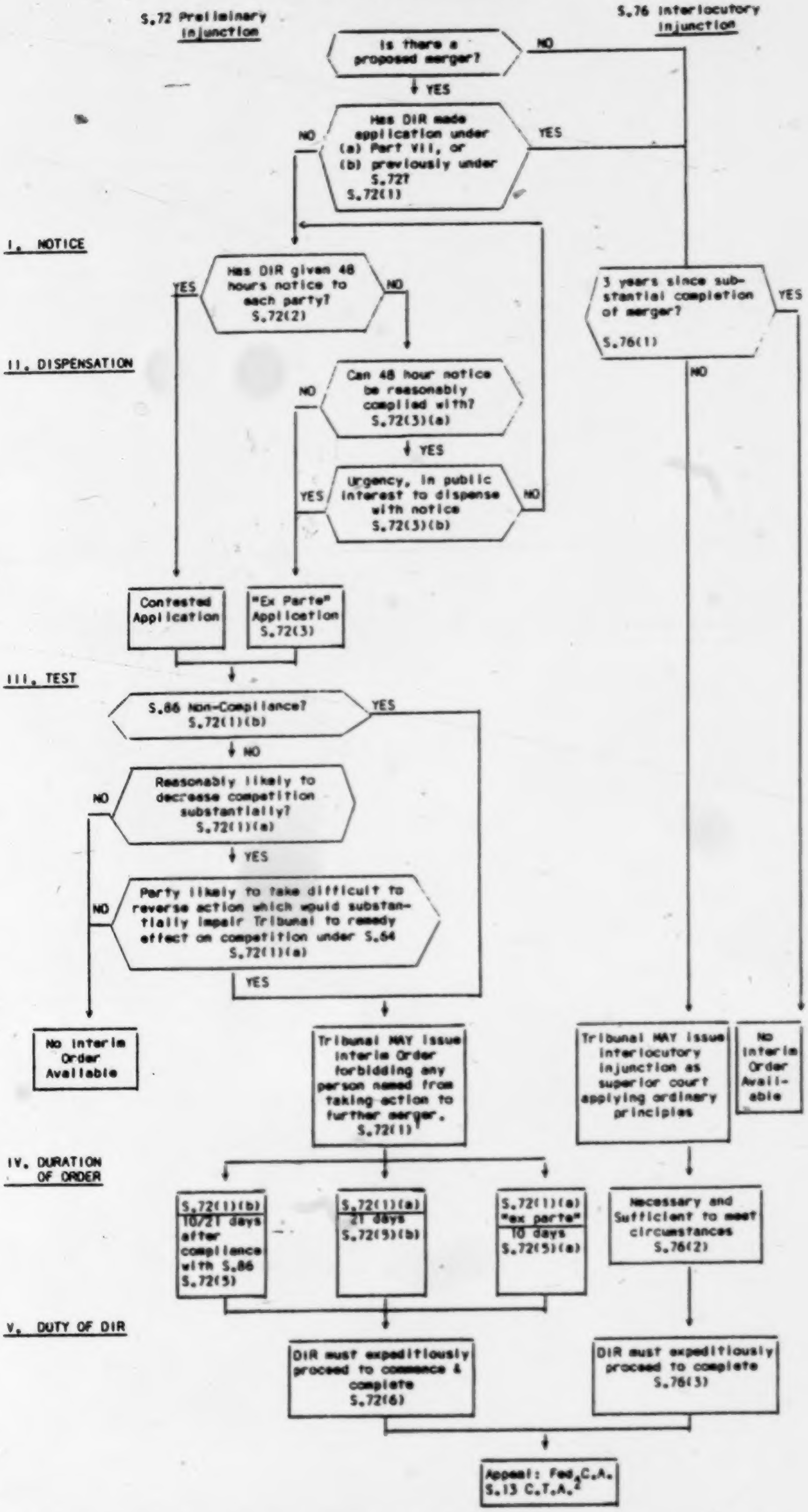
[1] See discussion on interim injunctions infra.

[2] The transaction may still be challenged under section 64.

APPENDIX D

COMPETITION ACT, 1986

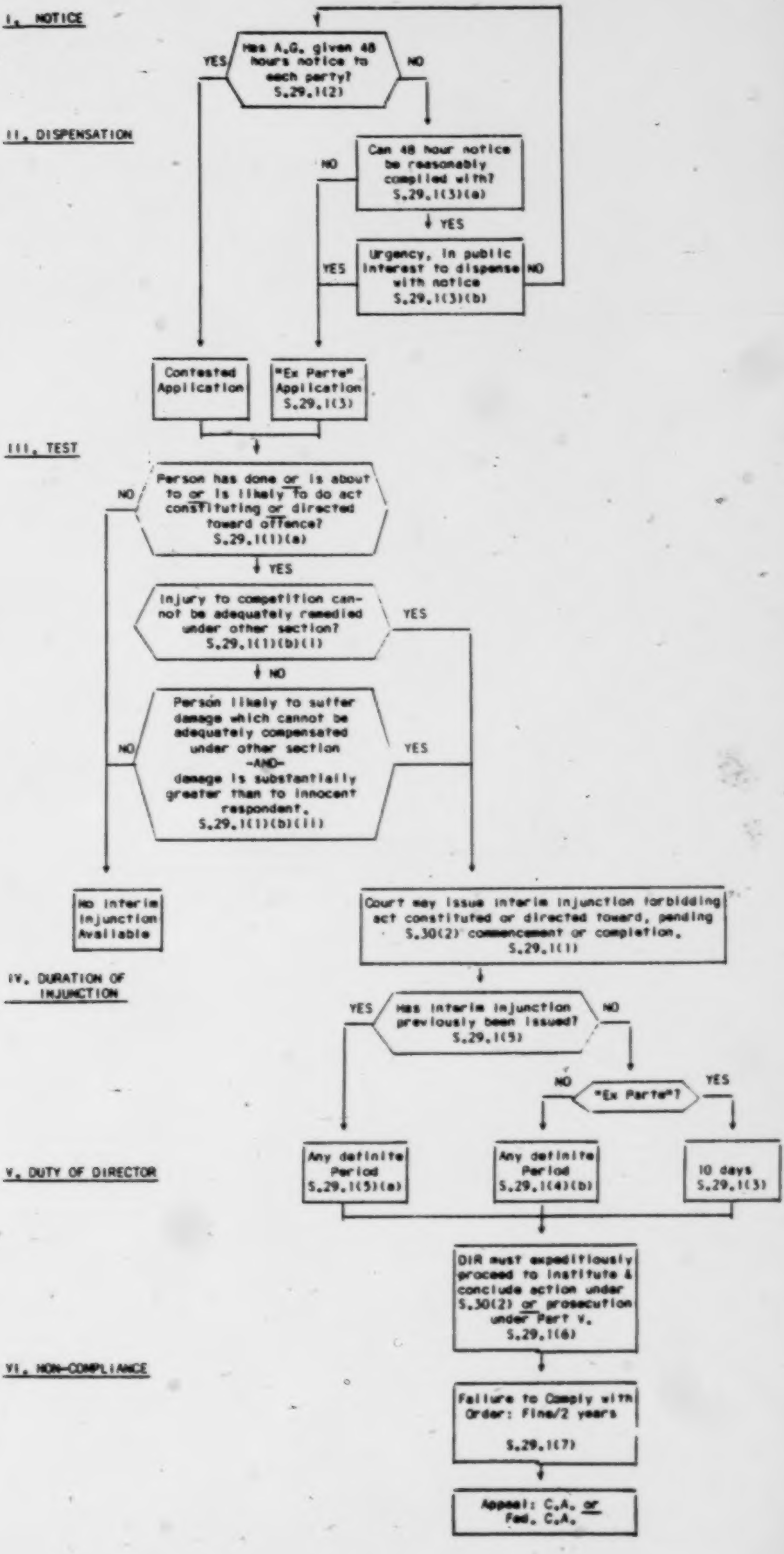
PROVISIONAL OR TEMPORARY INJUNCTIONS


S.72 Preliminary injunction
S.76 Interlocutory injunction
Is there a proposed merger?
NO
YES
Has DIR made application under (a) Part VII, or (b) previously under S.72? S.72(1)
NO
YES
I. NOTICE
Has DIR given 48 hours notice to each party? S.72(2)
YES
NO
II. DISPENSATION
Can 48 hour notice be reasonably complied with? S.72(3)(a)
NO
YES
Urgency, in public interest to dispense with notice S.72(3)(b)
YES
NO
3 years since substantial completion of merger? S.76(1)
YES
NO
Contested Application
"Ex Parte" Application S.72(3)
III. TEST
S.86 Non-Compliance? S.72(1)(b)
YES
NO
Reasonably likely to decrease competition substantially? S.72(1)(a)
NO
YES
Party likely to take difficult to reverse action which would substantially impair Tribunal to remedy effect on competition under S.64 S.72(1)(a)
NO
YES
No Interim Order Available
Tribunal MAY issue interim Order forbidding any person named from taking action to further merger. S.72(1)¹
Tribunal MAY issue interlocutory injunction as superior court applying ordinary principles
No Interim Order Available
IV. DURATION OF ORDER
S.72(1)(b) 10/21 days after compliance with S.86 S.72(5)
S.72(1)(a) 21 days S.72(5)(b)
S.72(1)(a) "ex parte" 10 days S.72(5)(a)
Necessary and Sufficient to meet circumstances S.76(2)
V. DUTY OF DIR
DIR must expeditiously proceed to commence & complete S.72(6)
DIR must expeditiously proceed to complete S.76(3)
Appeal: Fed.C.A. S.13 C.T.A.²

---

[1] S.72(6) requires the DIR to expeditiously proceed to commence and complete an application under S.64 if a preliminary injunction is obtained under S.72(1)(a).

[2] C.T.A. - Competition Tribunal Act


I. NOTICE
Has A.G. given 48 hours notice to each party? S.29.1(2)
YES
NO
II. DISPENSATION
Can 48 hour notice be reasonably complied with? S.29.1(3)(a)
NO
YES
Urgency, in public interest to dispense with notice S.29.1(3)(b)
YES
NO
Contested Application
"Ex Parte" Application S.29.1(3)
III. TEST
Person has done or is about to or is likely to do act constituting or directed toward offence? S.29.1(1)(a)
NO
YES
Injury to competition cannot be adequately remedied under other section? S.29.1(1)(b)(i)
YES
NO
Person likely to suffer damage which cannot be adequately compensated under other section -AND- damage is substantially greater than to innocent respondent. S.29.1(1)(b)(ii)
NO
YES
No interim injunction Available
Court may issue interim injunction forbidding act constituted or directed toward, pending S.30(2) commencement or completion. S.29.1(1)
IV. DURATION OF INJUNCTION
Has interim injunction previously been issued? S.29.1(5)
YES
NO
"Ex Parte"?
NO
YES
Any definite Period S.29.1(5)(a)
Any definite Period S.29.1(4)(b)
10 days S.29.1(3)
V. DUTY OF DIRECTOR
DIR must expeditiously proceed to institute & conclude action under S.30(2) or prosecution under Part V. S.29.1(6)
VI. NON-COMPLIANCE
Failure to Comply with Order: Fine/2 years S.29.1(7)
Appeal: C.A. or Fed. C.A.

APPENDIX E

MATHEMATICAL PROOFS

$$\text{Proof: } HHI = \Sigma s_i^2 + \frac{1}{N}$$

1. Before proving this essential relationship, it is necessary to appreciate the meaning of the following concepts:

$$S_i = \text{market share of firm } i \qquad (1)$$

$$\sum_{i=1}^{N} S_i = 1\text{, where } N = \text{number of firms} \qquad (2)$$

$$\text{Mean: } \bar{S} = \frac{\sum_{i=1}^{N} S_i}{N} = \frac{1}{N} \qquad (3)$$

$$\text{Deviation: } s_i = S_i - \bar{S} \qquad (4)$$

$$\text{Standard Deviation: } \sigma = \sqrt{\frac{\Sigma(S_i-\bar{S})^2}{N}} \qquad (5)$$

$$\text{Variance: } \sigma^2 = \frac{\Sigma(S_i-\bar{S})^2}{N} \qquad (6)$$

$$\text{Coefficient of Variation: } V = \frac{\sigma}{\bar{S}}$$

2. By definition, the standard deviation equals:

$$\sigma = \sqrt{\frac{\Sigma(S_i-\bar{S})^2}{N}} \qquad \text{(definition)}$$

$$= \sqrt{\frac{\Sigma S_i{}^2 - 2\Sigma S_i\bar{S} + \Sigma\bar{S}^2}{N}}$$

$$= \sqrt{\frac{HHI - 2\Sigma S_i\bar{S} + \Sigma\bar{S}^2}{N}} \qquad (HHI = \Sigma S_i^2)$$

$$= \sqrt{\frac{HHI - 2/N + \Sigma\bar{S}^2}{N}} \quad , \qquad \bar{S} = 1/N \quad \Sigma S_i = 1$$

$$= \sqrt{\frac{HHI - 2/N + 1/N}{N}} \quad , \qquad \Sigma\bar{S}^2 = N\bar{S}^2$$

$$= \sqrt{\frac{(HHI) \cdot N - 1}{N^2}}$$

$$= \frac{\sqrt{(HHI)N-1}}{N} \qquad (7)$$

3. Substituting the value of σ in equation (7) and the value of $\bar{S}$ in equation (3) into the definition of V in equation (6) yields:

$$V = \frac{\sigma}{\bar{S}}$$

$$= \sigma \cdot N$$

$$= \sqrt{(HHI) \cdot N - 1}$$

4. Squaring both sides,

$$V^2 = (HHI) \cdot N - 1$$

or,

$$HHI = \frac{V^2 + 1}{N} \qquad (8)$$

5. By rearranging equation (8),

$$HHI = \frac{(\sigma/\bar{S})^2 + 1}{N}$$

$$= \frac{\left(\frac{\Sigma s_i^2 / N}{1 / N^2}\right) + 1}{N}$$

$$= \frac{\left(\Sigma s_i^2\right) \cdot N + 1}{N}$$

Thus, $HHI = \Sigma s_i^2 + \frac{1}{N}$. (9) q.e.d

Proof: $L = 1 / \eta_1^D$

1. From the definition of profits (Π)

$$\Pi = TR - TC$$

$$= P(Q) \cdot Q - C(Q)$$

where TR is total revenue, TC and C(Q) are total costs.

2. Maximize Π by equating the derivative of Π with respect to Q:

$$\frac{d\Pi}{dQ} = \frac{\delta P}{\delta P} \cdot Q + \frac{\delta Q}{\delta P} \cdot P - \frac{\delta C}{Q} = 0$$

3. Substituting: (a) $\frac{\delta C}{\delta Q} = MC$,

(b) $-\frac{\delta P \cdot Q}{\delta Q \cdot P} = \frac{1}{\eta_1^D}$

4. $$P \left(1 - \frac{1}{\eta_1^D}\right) - MC = 0$$

$$\frac{P - MC}{P} = \frac{1}{\eta_1^D}$$

5.- Or, $L = \frac{P - MC}{P} = \frac{1}{\eta_1^D}$, where $n_1^D < 0$.

Proof: $$\eta_1^D = \frac{\eta_m^D}{S_1} + \frac{\eta_j^S\,(1-S_1)}{S_1}$$

1. Employing the "residual" demand hypothesis:

$$Q_1^D = Q_M^D - Q_j^S$$

where Q_1^D - demand for dominant firm

Q_m^D - demand for market

Q_j^S - supply of fringe.

2. Differenting with respect to P:

$$\frac{\delta Q_1^D}{\delta P} = \frac{\delta Q_m^D}{\delta P} - \frac{\delta Q_j^S}{\delta P} .$$

3. Multiplying by $-\frac{P}{Q_1^D}$,

$$\eta_1^D = -\frac{\delta Q_m^D}{\delta P} \cdot \frac{P}{Q_1^D} + \frac{\delta Q_1^S}{\delta P} \cdot \frac{P}{Q_1^D} .$$

4. Multiplying the first term by $\frac{Q_m^D}{Q_m^D}$, the second by $\frac{Q_j^S}{Q_j^S}$ yields,

$$\eta_1^D = \left(- \frac{\delta Q_m^D}{\delta P} \cdot \frac{P}{Q_m^D} \cdot \frac{Q_m^D}{Q_1^D} \right) + \left(\frac{\delta Q_j^S}{\delta P} \cdot \frac{P}{Q_j^S} \cdot \frac{Q_j^S}{Q_1^D} \right).$$

5. Noting that $S_1 = \frac{Q_1^D}{Q_m^D}$, $\frac{Q_j^S}{Q_1^D} = \frac{(1-S_1)}{S_1}$, $\eta_1^D = \frac{\eta_m^D}{S_1} + \frac{\eta_j^S\,(1-S_1)}{S_1}$ q.e.d.

The Calculation of Incremental Market Power

1. From the definition of the Lerner index,

$$\frac{P}{MC} = \frac{\eta_i^D}{\eta_i^D - 1}.$$

2. Assume, as a result of the merger, that marginal cost MC, market elasticity of demand η_m^D and fringe elasticity of supply η_j^S do not change.

3. The incremental effect on market power is,

$$\frac{P'-P}{P} = \frac{\eta_i^{D\prime} / (\eta_i^{D\prime}-1) - \eta_i^D\ (\eta_i^D-1)}{\eta_i^D\ (\eta_i^D-1)},$$

where the superscript (') denotes post-merger variables.

4. Substituting $\eta_i^D = \dfrac{\eta_m^D}{S_i} + \dfrac{\eta_j^S\ (1-S_i)}{S_i}$,

$$\frac{P'-P}{P} = \frac{S' - S\left(\eta_m^D + (1-S')\eta_j^S\right) / \left(\eta_m^D + (1-S)\eta_j^S\right)}{\eta_m^D + (1-S')\eta_j^S - S'}$$

where S is the market share of the larger pre-merger firm.

APPENDIX F

TRANSLATION OF HHI INTO CORRESPONDING RANGES OF OTHER INDICATORS[1]

This appendix is read as follows. In a market that has a Herfindahl Index of 3900, the lowest possible CR4 is 65% (0.65) and it is achieved when the market is composed of one firm with a 62% (0.62) share and 38 firms each having a 1% share; the highest possible CR4 is 90% (0.90) and it is achieved when the market is composed of two firms each having a 44% (0.44) share and 12 firms each having a 1% share.

	Lowest possible CR4 and other indicators			*Highest possible CR4 and other indicators*		
Herfindahl Index[b]	*CR4 (%)*	*Market share of the number one firm (%)*	*Number of other firms*	*CR4 (%)*	*Market share of each of the top X firms*[c] *(%)*	*Number of other firms*
300	18	15	85	30	8	70
600	26	23	77	47	12	53
900	32	29	71	59	15	41
1200	37	34	66	68	17	32
1500	41	38	62	77	19	23
1800	45	42	58	84	21	16
2100	48	45	55	91	23	9
2400	51	48	52	98	24	2
2700	54	51	49	91	30	10
3000	57	54	46	96	32	5
3300	60	57	43	100	33	0[d]
3600	63	60	40	87	42	15
3900	65	62	38	90	44	12
4200	68	65	35	94	46	8
4500	70	67	33	97	47	5
4800	72	69	31	100	49	2
5100	74	71	29	74	71	29
5400	76	73	27	76	73	27
5700	78	75	25	78	75	25
6000	80	77	23	80	77	23
6300	82	79	21	82	79	21
6600	84	81	19	84	81	19
6900	86	83	17	86	83	17
7200	88	85	15	88	85	15
7500	90	87	13	90	87	13
7800	91	88	12	91	88	12
8100	93	90	10	93	90	10
8400	95	92	8	95	92	8
8700	96	93	7	96	93	7
9000	98	95	5	98	95	5
9300	99	96	4	99	96	4
9600	100	98	2	100	98	2
9900	100	99	0[d]	100	99	0[d]

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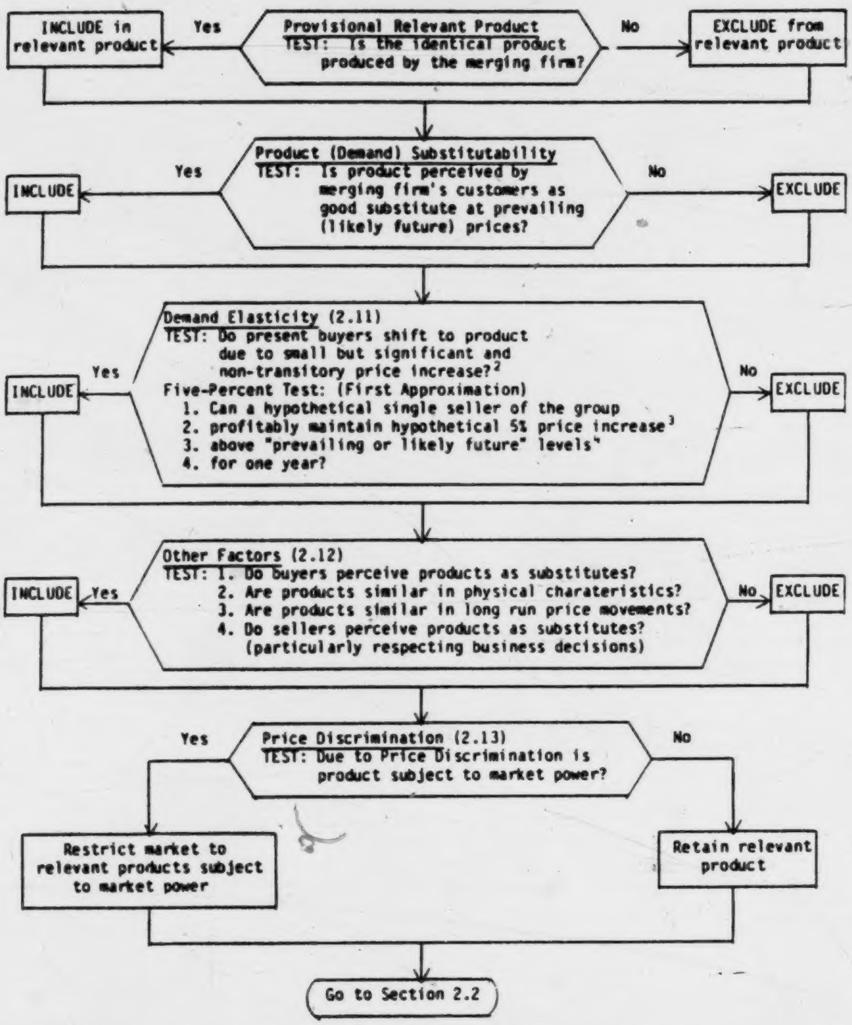
[1] This table has been borrowed from, D.S. Weinstock, "Some Little-Known Properties of the Herfindahl-Hirschman Index: Problems of Translation And Specification", Winter (1984) 29 Antitrust Bulletin 705, at p. 716.

APPENDIX G

FLOWCHART OF 1984 MERGER GUIDELINES

1984 Merger Guidelines
Section 2.1
2.1 Product Market Definition
(Determination of Relevant Product)[1]


INCLUDE in relevant product
Yes
Provisional Relevant Product TEST: Is the identical product produced by the merging firm?
No
EXCLUDE from relevant product
INCLUDE
Yes
Product (Demand) Substitutability TEST: Is product perceived by merging firm's customers as good substitute at prevailing (likely future) prices?
No
EXCLUDE
INCLUDE
Yes
Demand Elasticity (2.11) TEST: Do present buyers shift to product due to small but significant and non-transitory price increase?[2]
Five-Percent Test: (First Approximation)
1. Can a hypothetical single seller of the group
2. profitably maintain hypothetical 5% price increase[3]
3. above "prevailing or likely future" levels[4]
4. for one year?
No
EXCLUDE
INCLUDE
Yes
Other Factors (2.12) TEST: 1. Do buyers perceive products as substitutes?
2. Are products similar in physical charateristics?
3. Are products similar in long run price movements?
4. Do sellers perceive products as substitutes? (particularly respecting business decisions)
No
EXCLUDE
Yes
Price Discrimination (2.13) TEST: Due to Price Discrimination is product subject to market power?
No
Restrict market to relevant products subject to market power
Retain relevant product
Go to Section 2.2

NOTE: All references to the Merger Guidelines refer to the Trade Regulation Reports, Commerce Clearing House:
1984 - 4490
1982 - 4500
1968 - 4510

---

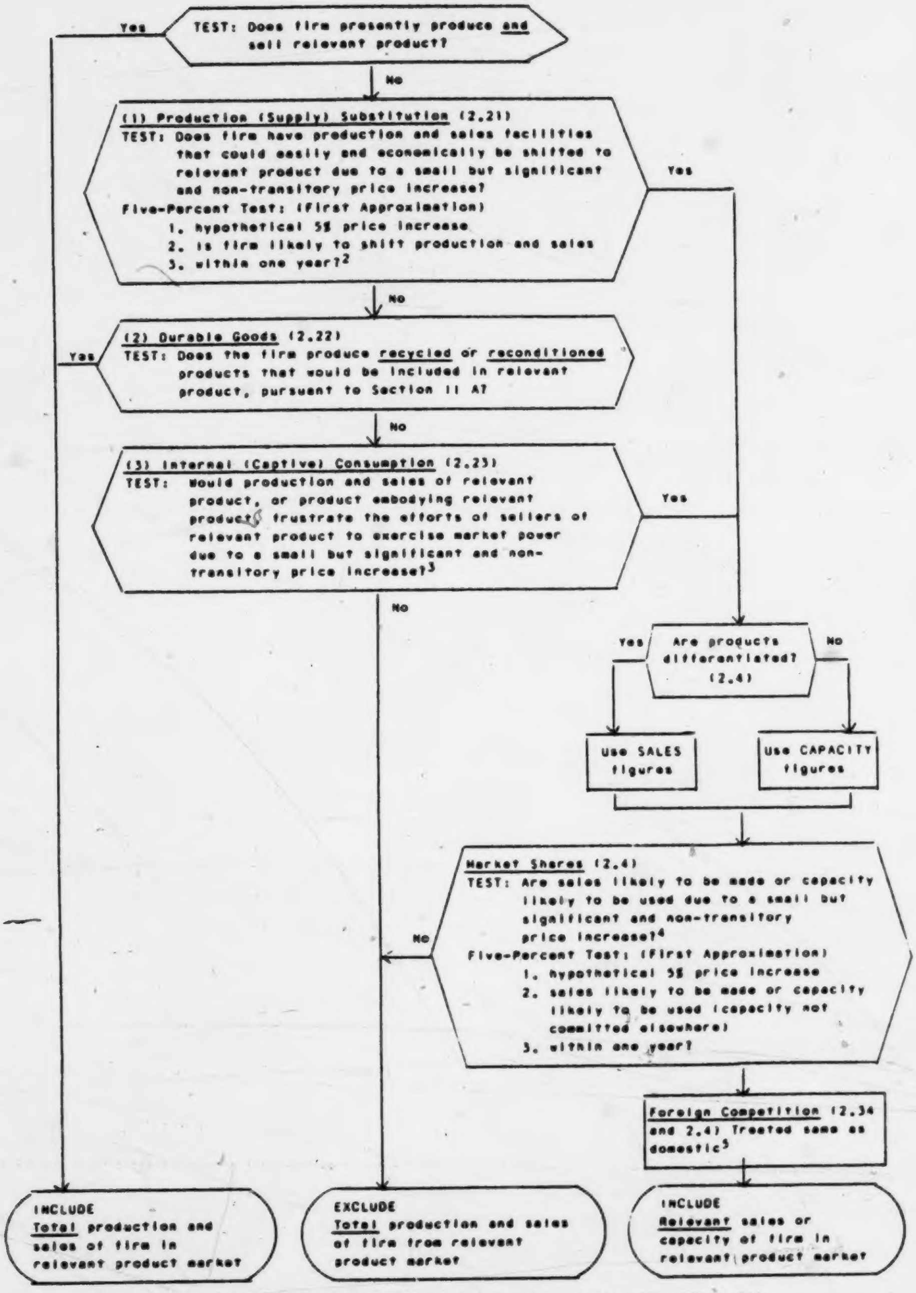
[1] Relevant Product - all products that will be included in the market collectively

[2] This may be based on circumstantial evidence. See: note 10, Section II, 1982 Guidelines.

[3] The "price" is the price of the product. See: 4492.101, note 6. Buyers and sellers immediately recognize the price increase and believe it will be maintained in the future. See 4492.101 (1984); note 10 (1982).

[4] Future prices will be used "when changes in the prevailing prices can be predicted with reasonable reliability". 4492.101 (1984).

1984 Merger Guidelines
Section 2.2 and 2.4
2.2 Identification of Firms that Produce the Relevant Product
2.4 Calculating Market Shares
(Determination of Relevant Product *Market*)[1]


TEST: Does firm presently produce and sell relevant product?
Yes
No
(1) Production (Supply) Substitution (2.21)
TEST: Does firm have production and sales facilities that could easily and economically be shifted to relevant product due to a small but significant and non-transitory price increase?
Five-Percent Test: (First Approximation)
1. hypothetical 5% price increase
2. is firm likely to shift production and sales
3. within one year?[2]
Yes
No
(2) Durable Goods (2.22)
TEST: Does the firm produce recycled or reconditioned products that would be included in relevant product, pursuant to Section II A?
Yes
No
(3) Internal (Captive) Consumption (2.23)
TEST: Would production and sales of relevant product, or product embodying relevant products frustrate the efforts of sellers of relevant product to exercise market power due to a small but significant and non-transitory price increase?[3]
Yes
No
Are products differentiated? (2.4)
Yes
No
Use SALES figures
Use CAPACITY figures
Market Shares (2.4)
TEST: Are sales likely to be made or capacity likely to be used due to a small but significant and non-transitory price increase?[4]
Five-Percent Test: (First Approximation)
1. hypothetical 5% price increase
2. sales likely to be made or capacity likely to be used (capacity not committed elsewhere)
3. within one year?
No
Foreign Competition (2.34 and 2.4) Treated same as domestic[5]
INCLUDE Total production and sales of firm in relevant product market
EXCLUDE Total production and sales of firm from relevant product market
INCLUDE Relevant sales or capacity of firm in relevant product market

---

[1] Relevant Product Market will be total sales or capacity which will form the denominator in determining market shares.

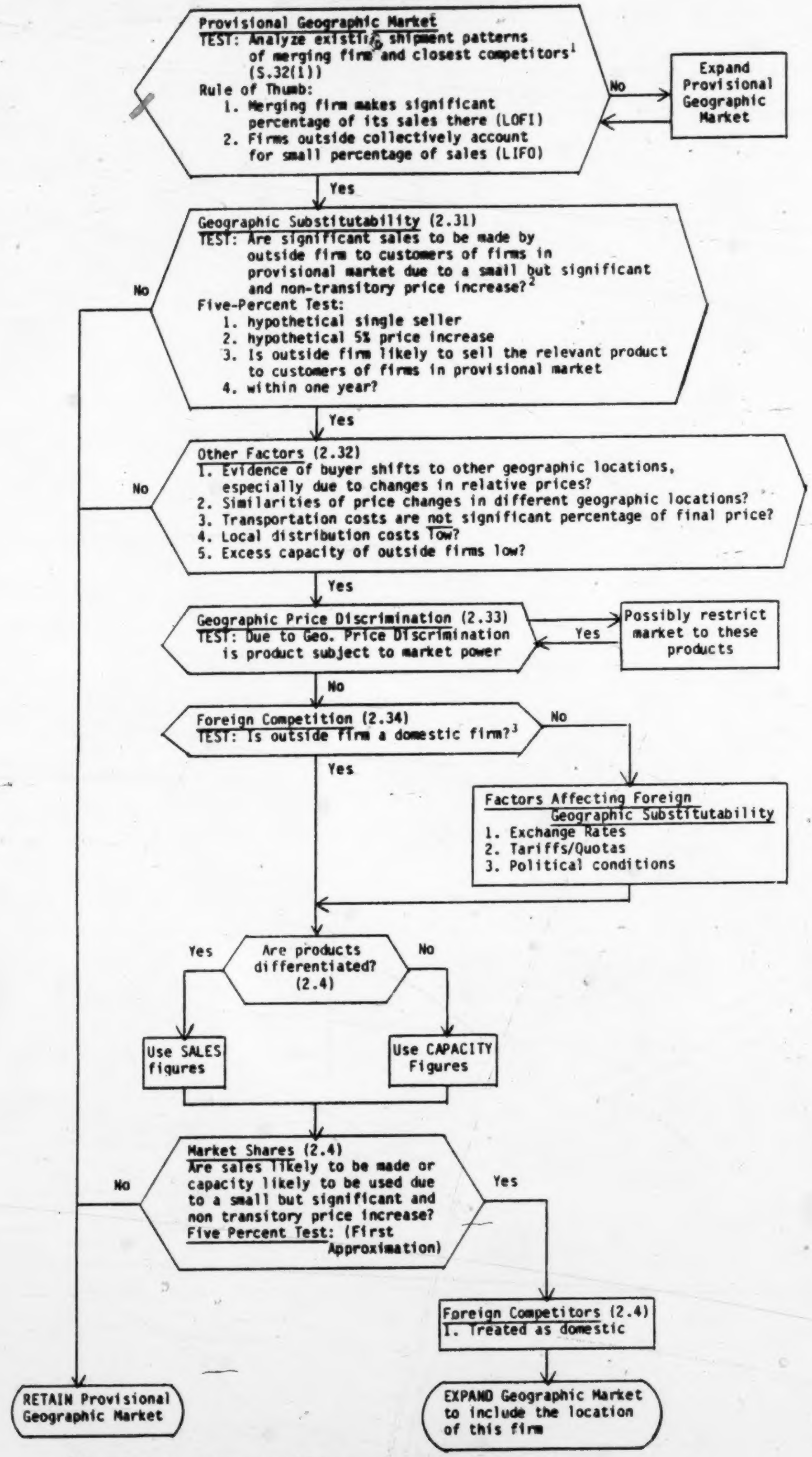
[2] The 1982 Guidelines set the duration of this test at 6 months.

[3] To be determined *prima facie* by Five-Percent Test.

[4] Capacity that is committed elsewhere, for example, would not be capable of responding to a price increase.

[5] See: 4492.40 for special features governing foreign competition.

1984 Merger Guidelines
Section 2.3 and 2.4
2.3 Geographic Market Definition
2.4 Calculating Market Shares


Provisional Geographic Market
TEST: Analyze existing shipment patterns of merging firm and closest competitors[1] (S.32(1))
Rule of Thumb:
1. Merging firm makes significant percentage of its sales there (LOFI)
2. Firms outside collectively account for small percentage of sales (LIFO)
No
Expand Provisional Geographic Market
Yes
Geographic Substitutability (2.31)
TEST: Are significant sales to be made by outside firm to customers of firms in provisional market due to a small but significant and non-transitory price increase?[2]
Five-Percent Test:
1. hypothetical single seller
2. hypothetical 5% price increase
3. Is outside firm likely to sell the relevant product to customers of firms in provisional market
4. within one year?
No
Yes
Other Factors (2.32)
1. Evidence of buyer shifts to other geographic locations, especially due to changes in relative prices?
2. Similarities of price changes in different geographic locations?
3. Transportation costs are not significant percentage of final price?
4. Local distribution costs low?
5. Excess capacity of outside firms low?
No
Yes
Geographic Price Discrimination (2.33)
TEST: Due to Geo. Price Discrimination is product subject to market power
Yes
Possibly restrict market to these products
No
Foreign Competition (2.34)
TEST: Is outside firm a domestic firm?[3]
No
Factors Affecting Foreign Geographic Substitutability
1. Exchange Rates
2. Tariffs/Quotas
3. Political conditions
Yes
Are products differentiated? (2.4)
Yes
No
Use SALES figures
Use CAPACITY Figures
Market Shares (2.4)
Are sales likely to be made or capacity likely to be used due to a small but significant and non transitory price increase?
Five Percent Test: (First Approximation)
No
Yes
Foreign Competitors (2.4)
1. Treated as domestic
RETAIN Provisional Geographic Market
EXPAND Geographic Market to include the location of this firm

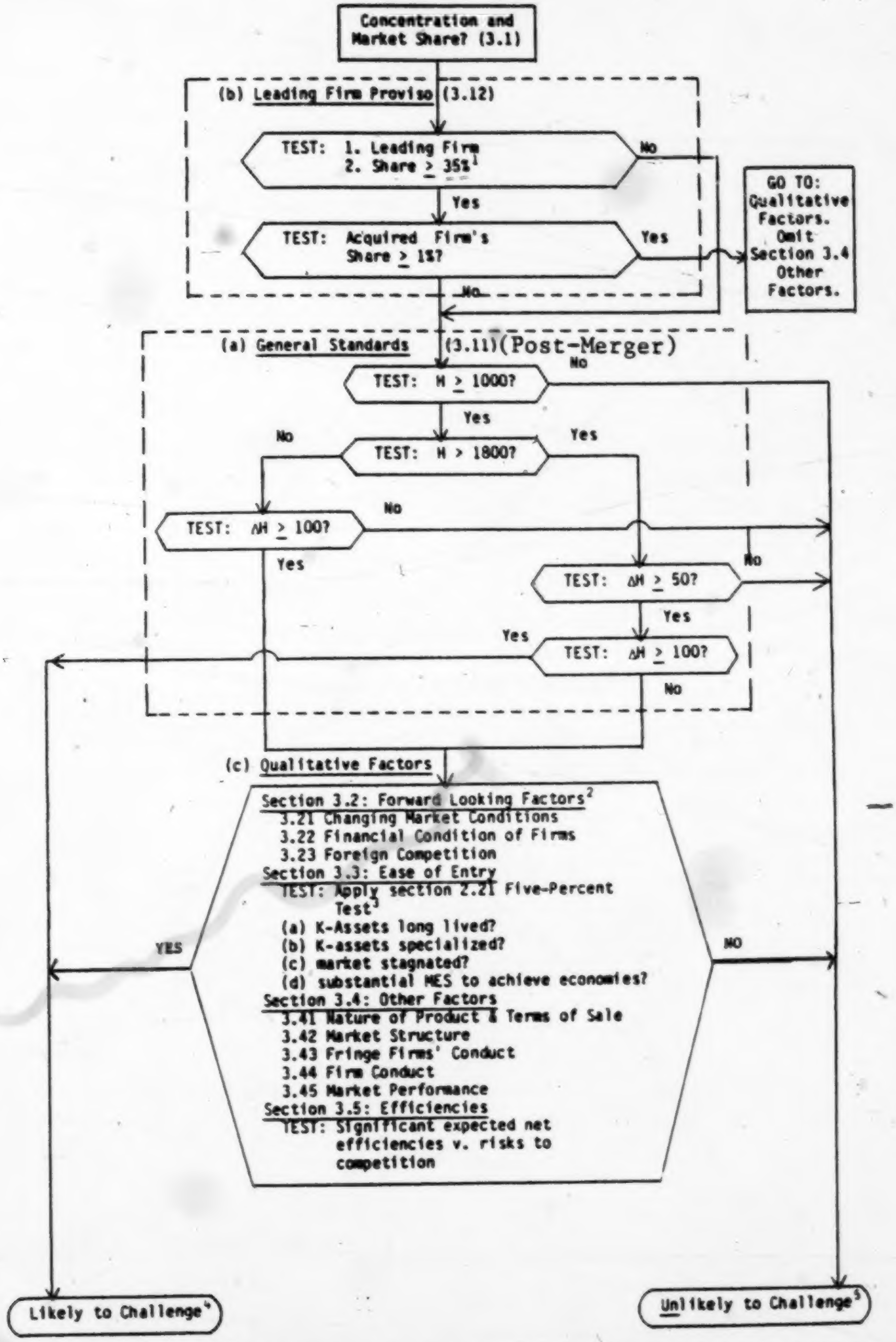
---

[1] Location of sellers, not buyers.

[2] This test is similar to a demand substitutability test where the issue arises as to whether or not buyers will shift to outside firms. In addition, the barrier to entry problem is addressed further in Section 3.3. As in the product market definition, the "smallest market" principle will apply. See: 4492.301 (1984).

[3] The effects of foreign competition have been expanded from the 1982 Guidelines. See: *infra*, Section 3.23 (Special Factors Affecting Foreign Firms).

1984 Merger Guidelines
Horizontal Mergers
Section 3


Concentration and Market Share? (3.1)
(b) Leading Firm Proviso (3.12)
TEST: 1. Leading Firm 2. Share $\geq$ 35%[1]
No
Yes
TEST: Acquired Firm's Share $\geq$ 1%?
Yes
No
GO TO: Qualitative Factors. Omit Section 3.4 Other Factors.
(a) General Standards (3.11)(Post-Merger)
TEST: $H \geq 1000$?
No
Yes
TEST: $H > 1800$?
No
Yes
TEST: $\Delta H \geq 100$?
No
Yes
TEST: $\Delta H \geq 50$?
No
Yes
TEST: $\Delta H \geq 100$?
Yes
No
(c) Qualitative Factors
Section 3.2: Forward Looking Factors[2]
3.21 Changing Market Conditions
3.22 Financial Condition of Firms
3.23 Foreign Competition
Section 3.3: Ease of Entry
TEST: Apply section 2.21 Five-Percent Test[3]
(a) K-Assets long lived?
(b) K-assets specialized?
(c) market stagnated?
(d) substantial MES to achieve economies?
Section 3.4: Other Factors
3.41 Nature of Product & Terms of Sale
3.42 Market Structure
3.43 Fringe Firms' Conduct
3.44 Firm Conduct
3.45 Market Performance
Section 3.5: Efficiencies
TEST: Significant expected net efficiencies v. risks to competition
YES
NO
Likely to Challenge[4]
Unlikely to Challenge[5]

---

[1] The requirement that the leading firm have twice the market share of the second largest firm has been dropped from the 1982 Guidelines. See: 4503.102.

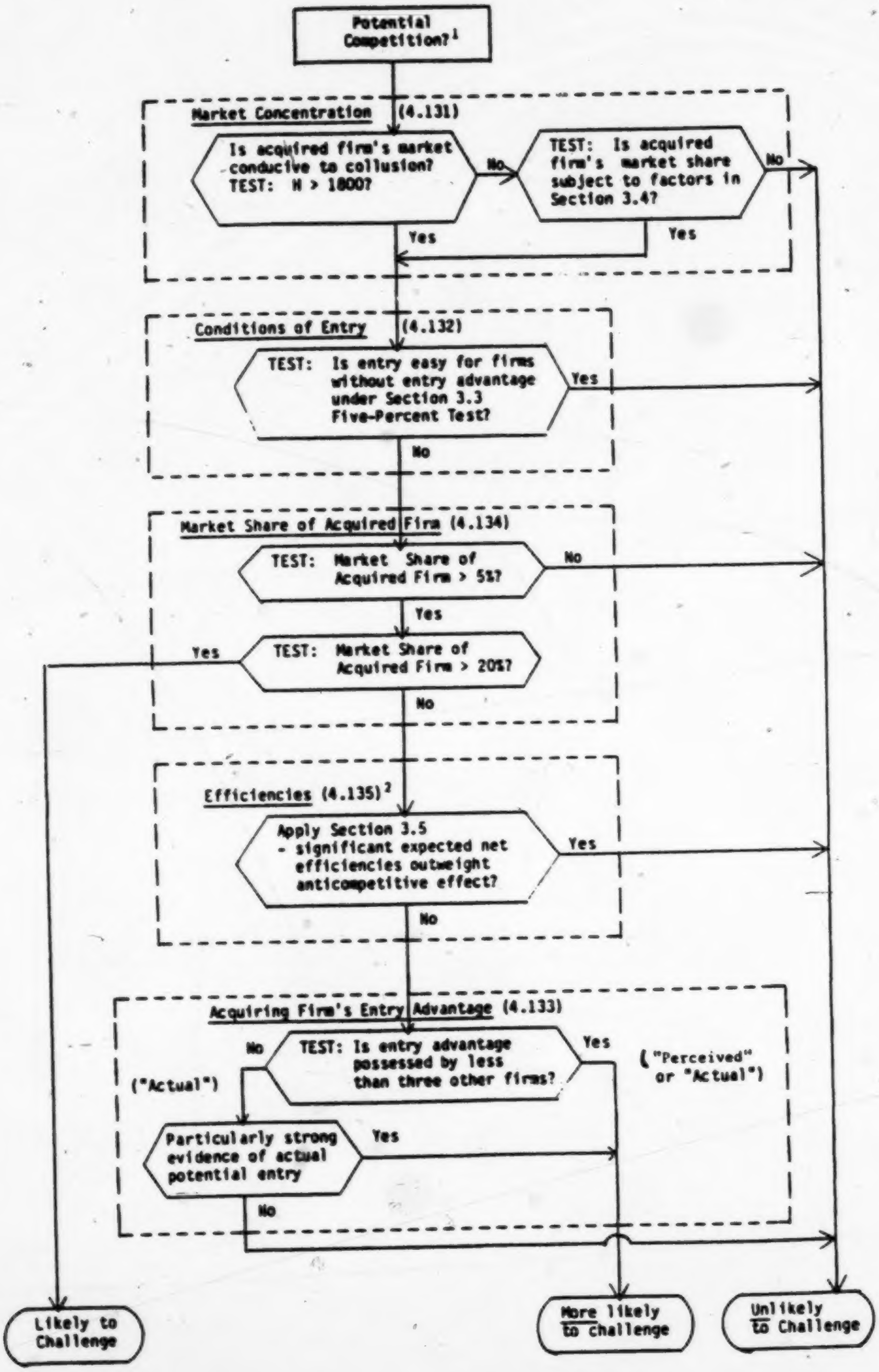
[2] Sections 3.2 and 3.5 were not included in the 1982 Guidelines.

[3] A two year time period will generally be used. This section is concerned with (a) significant modifications to existing facilities or (b) construction of new facilities. See: 4493.30.

[4] Except in "extraordinary circumstances". See: 4493.101(c).

[5] Except in "extraordinary circumstances". See: 4493.101(a). If $H < 1000$, DOJ will not challenge 1982 Guidelines stated the DOJ was "unlikely" to challenge.

1984 Merger Guidelines
Horizontal Effect from Non-Horizontal Mergers (Vertical & Conglomerate)
Section 4.1

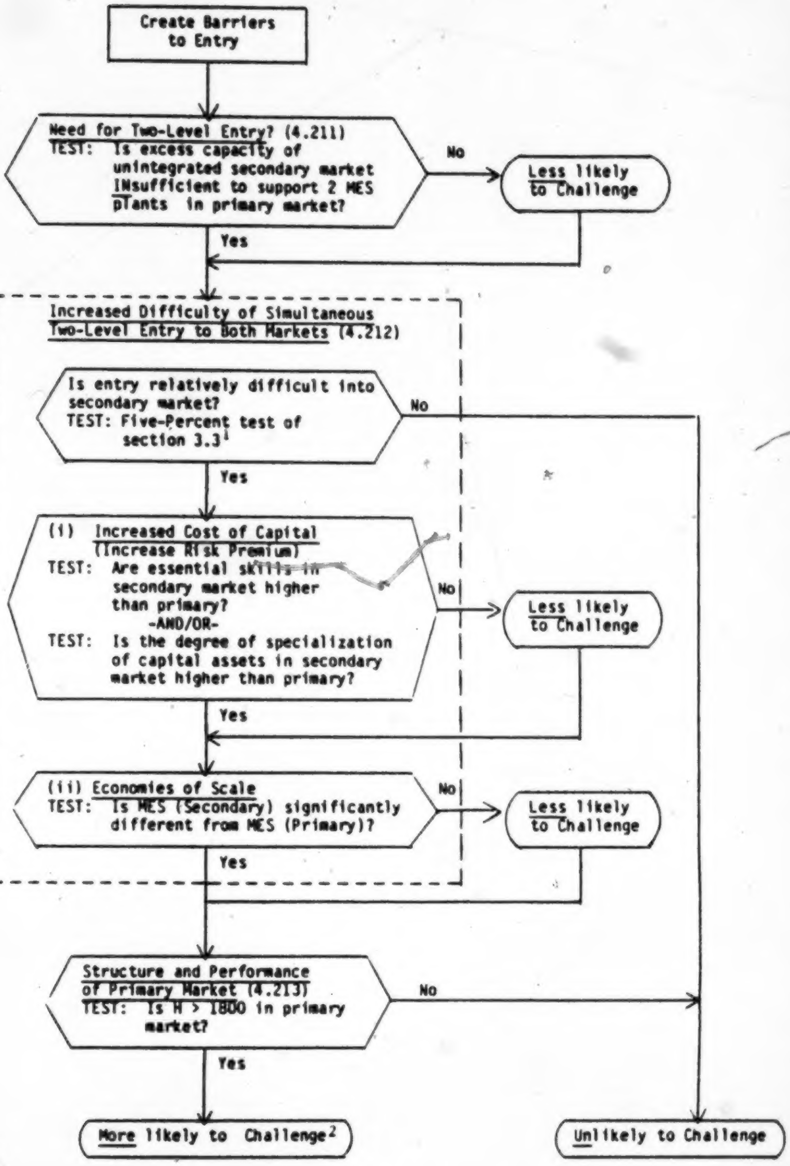

Potential Competition?[1]
Market Concentration (4.131)
Is acquired firm's market conducive to collusion? TEST: H > 1800?
No
TEST: Is acquired firm's market share subject to factors in Section 3.4?
No
Yes
Yes
Conditions of Entry (4.132)
TEST: Is entry easy for firms without entry advantage under Section 3.3 Five-Percent Test?
Yes
No
Market Share of Acquired Firm (4.134)
TEST: Market Share of Acquired Firm > 5%?
No
Yes
TEST: Market Share of Acquired Firm > 20%?
Yes
No
Efficiencies (4.135)[2]
Apply Section 3.5 - significant expected net efficiencies outweight anticompetitive effect?
Yes
No
Acquiring Firm's Entry Advantage (4.133)
TEST: Is entry advantage possessed by less than three other firms?
No
("Actual")
Yes
("Perceived" or "Actual")
Particularly strong evidence of actual potential entry
Yes
No
Likely to Challenge
More likely to challenge
Unlikely to Challenge

---

[1] Perceived and Actual Potential Competition treated identically. Note: Acquired firm is firm in the market, acquiring firm is the potential entrant.

[2] Elevated from defence in 1982 Guidelines to "other Factor" in 1984 Guidelines.

1984 Merger Guidelines
Horizontal Effects from Non-Horizontal Mergers (Vertical)
Section 4.21

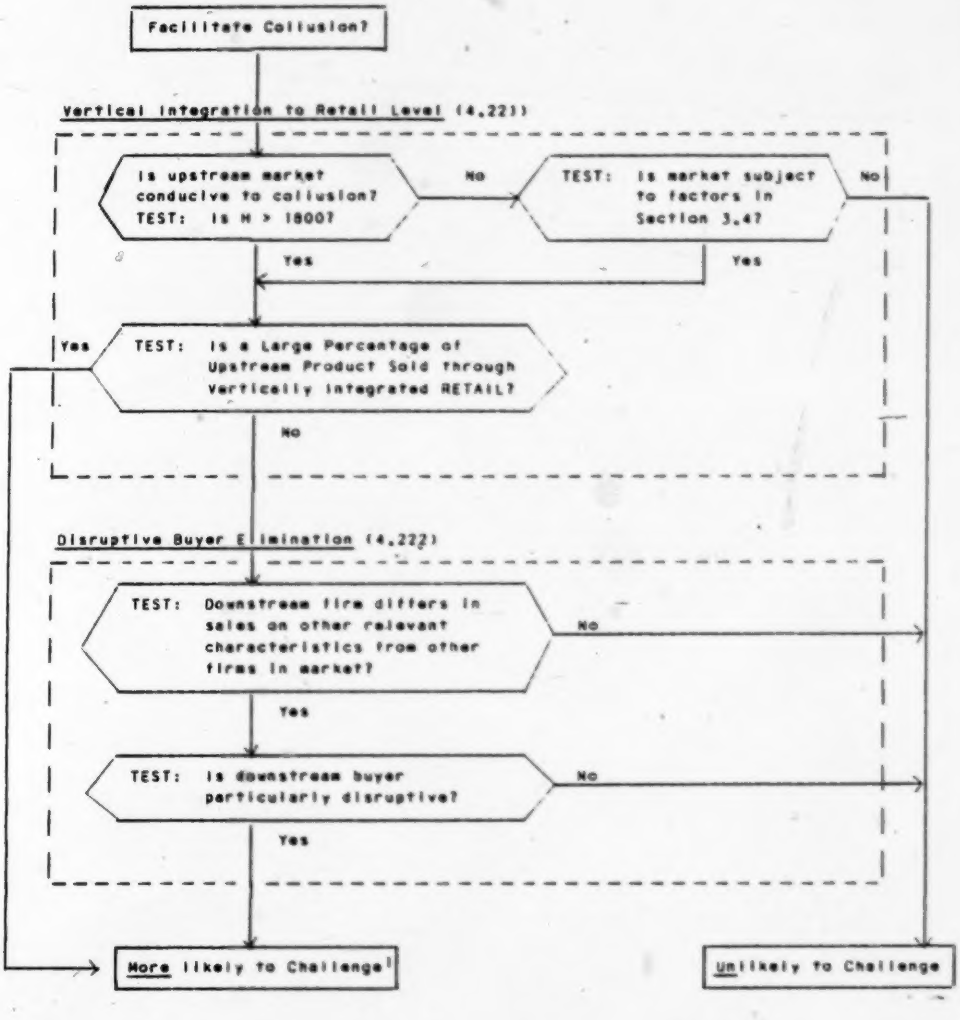

Create Barriers to Entry
Need for Two-Level Entry? (4.211)
TEST: Is excess capacity of unintegrated secondary market INsufficient to support 2 MES plants in primary market?
No
Less likely to Challenge
Yes
Increased Difficulty of Simultaneous Two-Level Entry to Both Markets (4.212)
Is entry relatively difficult into secondary market?
TEST: Five-Percent test of section 3.3¹
No
Yes
(i) Increased Cost of Capital (Increase Risk Premium)
TEST: Are essential skills in secondary market higher than primary?
-AND/OR-
TEST: Is the degree of specialization of capital assets in secondary market higher than primary?
No
Less likely to Challenge
Yes
(ii) Economies of Scale
TEST: Is MES (Secondary) significantly different from MES (Primary)?
No
Less likely to Challenge
Yes
Structure and Performance of Primary Market (4.213)
TEST: Is H > 1800 in primary market?
No
Yes
More likely to Challenge²
Unlikely to Challenge

---

[1] If entry can be accomplished under the conditions stated in section 3.3, then the DOJ will consider whether entry into the secondary market "significantly increase" the costs of entry into the primary market.

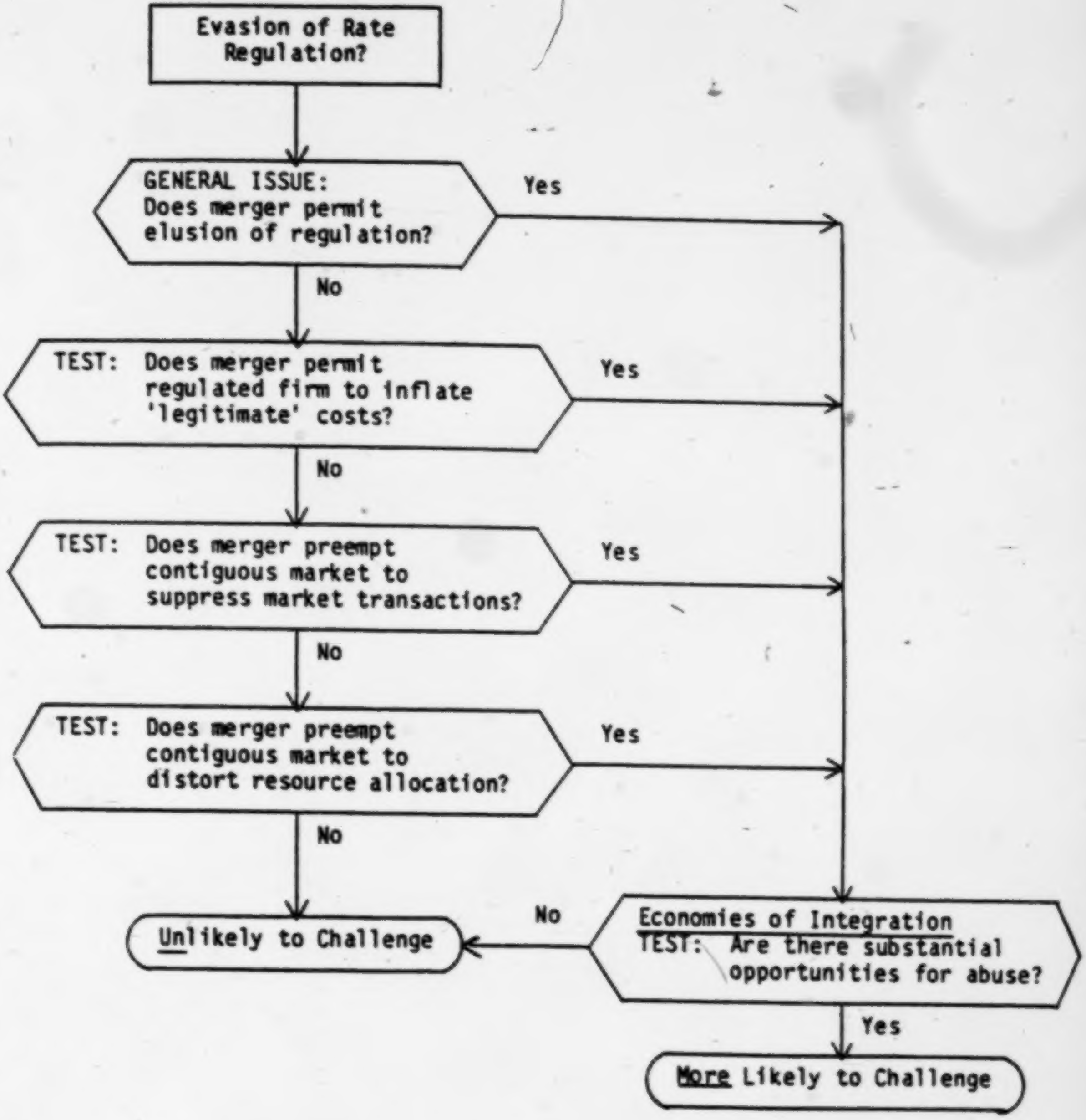
[2] Pursuant to §.4.24 Guidelines, the DOJ will give substantially more weight to efficiencies when challenging a vertical, rather than horizontal merger.

1984 Merger Guidelines
Horizontal Effects from Non-Horizontal Mergers (Vertical)
Section 4.22

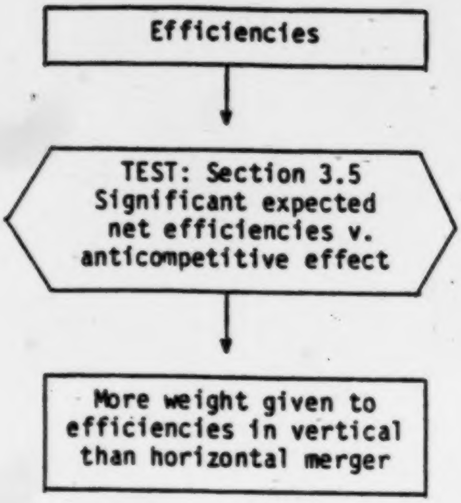

Facilitate Collusion?
Vertical Integration to Retail Level (4.221)
Is upstream market conducive to collusion? TEST: Is H > 1800?
No
TEST: Is market subject to factors in Section 3.4?
No
Yes
Yes
Yes
TEST: Is a Large Percentage of Upstream Product Sold through Vertically Integrated RETAIL?
No
Disruptive Buyer Elimination (4.222)
TEST: Downstream firm differs in sales on other relevant characteristics from other firms in market?
No
Yes
TEST: Is downstream buyer particularly disruptive?
No
Yes
More likely to Challenge[1]
Unlikely to Challenge

Pursuant to 8.4.24 Guidelines, the DOJ will give substantially more weight to efficiencies when challenging a vertical, rather than horizontal menger.

1984 Merger Guidelines
Horizontal Effects from Non-Horizontal Mergers (Vertical & Conglomerate)
Section 4.23


Evasion of Rate Regulation?
GENERAL ISSUE: Does merger permit elusion of regulation?
Yes
No
TEST: Does merger permit regulated firm to inflate 'legitimate' costs?
Yes
No
TEST: Does merger preempt contiguous market to suppress market transactions?
Yes
No
TEST: Does merger preempt contiguous market to distort resource allocation?
Yes
No
Unlikely to Challenge
No
Economies of Integration
TEST: Are there substantial opportunities for abuse?
Yes
More Likely to Challenge

1984 Merger Guidelines
Horizontal Effects from Non-Horizontal Mergers (Vertical & Conglomerate)
Section 4.24[1]


Efficiencies
TEST: Section 3.5
Significant expected net efficiencies v. anticompetitive effect
More weight given to efficiencies in vertical than horizontal merger

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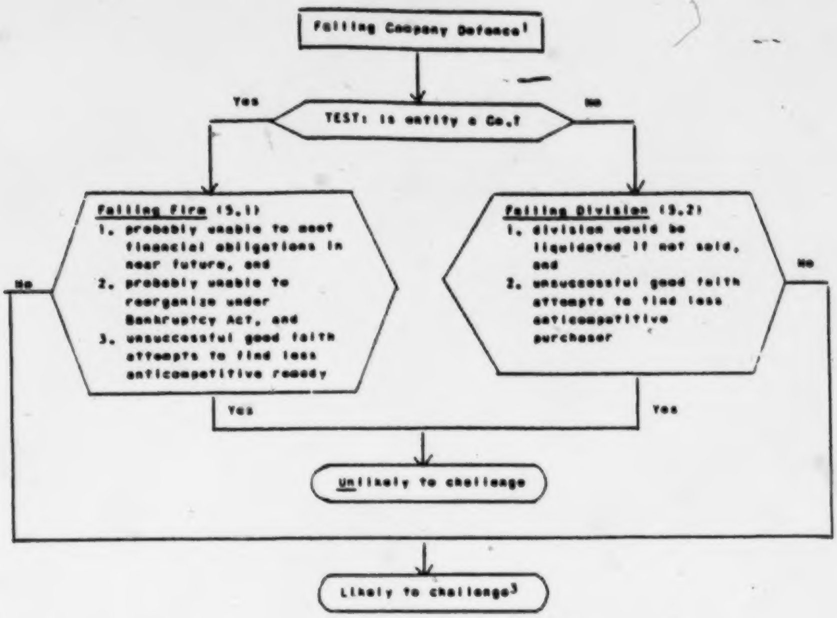
[1] This section was not specifically included under competitive problems from vertical mergers.

1984 Merger Guidelines
Defences
Section 5


Failing Company Defence[1]
Yes
TEST: Is entity a Co.?
No
Failing Firm (5.1)
1. probably unable to meet financial obligations in near future, and
2. probably unable to reorganize under Bankruptcy Act, and
3. unsuccessful good faith attempts to find less anticompetitive remedy
Failing Division (5.2)
1. division would be liquidated if not sold, and
2. unsuccessful good faith attempts to find less anticompetitive purchaser
No
No
Yes
Yes
Unlikely to challenge
Likely to challenge[3]

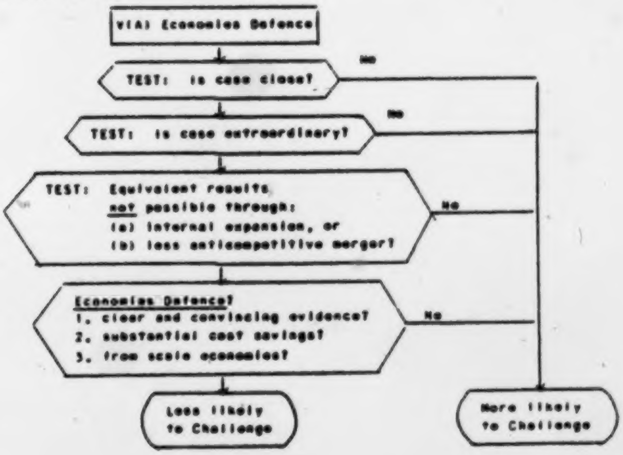
---

[1] Note: DOJ will construe this defence strictly.

[2] Under the 1982 Merger Guidelines, a third defence was available. The DOJ was unlikely to challenge an otherwise anticompetitive merger in which one of the merging firms was a financially healthy subdivision of an allegedly failing parent firm when:

> (1) the parent firm satisfies the above conditions, and (2) the competitive harm from the disappearance of the parent firm from its market would substantially outweigh the competitive harm threatened by the merger, (3) the proposed transaction probably would enable the parent firm to avoid bankruptcy or to reorganize successfully, (4) the third condition stated in the text also has been satisfied with respect to the healthy subdivision, and (5) the merging firm is not capable of independent existence as a business entity. Where the merging firm is capable of independent existence, the Division may insist that the parent company attempt to transfer common stock in it to the parent company's creditors.
>
> See: 4505.20, footnote 57.

[3] In addition to the "failing company" defence, the 1982 Merger Guidelines contained a weak efficiencies defence as follows:


V(A) Economies Defence
TEST: Is case close?
No
TEST: Is case extraordinary?
No
TEST: Equivalent results not possible through:
(a) internal expansion, or
(b) less anticompetitive merger?
No
Economies Defence?
1. clear and convincing evidence?
2. substantial cost savings?
3. from scale economies?
No
Less likely to Challenge
More likely to Challenge

See: 4505.10

DEPARTMENT OF JUSTICE MERGER GUIDELINES
COMPARISON OF 1968 AND 1982 HORIZONTAL MERGER STANDARDS
EXPRESSED IN HERFINDAHL-HIRSCHMAN INDEXES

SPECTRUM OF CONCENTRATION

		Highly Concentrated	Less Highly Concentrated	Unconcentrated
968	Pre-Merger Herfindahl-Hirschman Index	Approximately Greater than 2,000	Approximately Less than 2,000	—
982	Post-Merger Herfindahl-Hirschman Index	Greater than 1,800	Between 1,000-1,800	Less than 1,000

ENFORCEMENT STANDARD

		Highly Concentrated	Less Highly Concentrated	Unconcentrated
.968	DOJ Challenges if Change in Herfindahl-Hirschman Index is:	Greater than 30-40	Greater than 50-90	—
.982	DOJ Challenges if Change in Herfindahl-Hirschman Index is:	Greater than 100 Other factors considered if between 50-100	Other factors considered if greater than 100	—

DEPARTMENT OF JUSTICE MERGER GUIDELINES
COMPARISON OF 1968 AND 1982 HORIZONTAL MERGER STANDARDS
EXPRESSED IN FOUR-FIRM CONCENTRATION RATIOS

SPECTRUM OF CONCENTRATION

		Highly Concentrated	Less Highly Concentrated	Unconcentrated
1968	Pre-Merger Four-Firm Concentration Ratio	Greater than 75%	Less than 75%	——
1982	Post-Merger Four-Firm Concentration Ratio	Approximately Greater than 70%	Approximately Between 50-70%	Approximately Less than 50%

ENFORCEMENT STANDARD

		Highly Concentrated		Less Highly Concentrated		Unconcentrated	
		Acquiring Firm's Share is:	and Acquired Firm's Share is:	Acquiring Firm's Share is:	and Acquired Firm's Share is:	Acquiring Firm's Share is:	and Acquired Firm's Share is:
1968	DOJ Challenges if:	4% 10% 15% or more	4% or more 2% or more 1% or more	5% 10% 15% 20% 25% or more	5% or more 4% or more 3% or more 2% or more 1% or more	——	——
1982	DOJ Challenges if:	4% 10% 15% or more	6.2-12.5% or more 2.5-5% or more 1.7-3.3% or more	5% 10% 15% 20% 25% or more	10% or more 5% or more 3.3% or more 2.5% or more 2% or more	——	——

APPENDIX H

1984 Minor Amendments to the 1982 Merger Guidelines[1]

1. Market Definition:
    - (a) the "five percent test" is reworded so that firms could raise output to such a degree that they could prevent other firms from profitability raising price by five percent for one year. The emphasis is now on preventing a price increase; the 1982 Guidelines questioned whether substitution would be significant. (s.2.11)
    - (b) The price is the price of the product at the stage of the industry being examined. (s.2.11)
    - (c) The price will be the prevailing or likely future price, when it can be predicted reliably. (s.2.11)
    - (d) Price change may be larger or smaller than five percent. (s.2.11)
    - (e) Price movements only considered when not attributable to common cost factors. (s.2.12)
2. Market Measurement:
    - (a) Guidance is offered for choosing between sales or capacity measures. Sales are recommended when products are differentiated, capacity when

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[1] See: Peter Bronstee, "A Review of the Revised Merger Guidelines", (1984) 29 Antitrust Bulletin 613, at p. 631 for a summary of the 1984 revisions.

products are not. (s.2.4)

3. Statistical Criteria:
   - (a) Not only concentration measurements will be viewed in determining market power.[2] (s.3.11)
   - (b) The 1984 Guidelines "will not" challenge (1982 "unlikely") below the thresholds and "will challenge (1982 "likely") above the bright line. (s.3.11)
4. Other Qualitative Factors:
   - (a) Forward looking factors are included--market evolution, financial conditions and fringe supply. (s.3.2)
5. Defences:
   - (a) Efficiency defence transfer to qualitative factor.
   - (b) Healthy subdivision of a failing firm has been deleted as a footnote. This may mean that the DOJ may still entertain such an argument.

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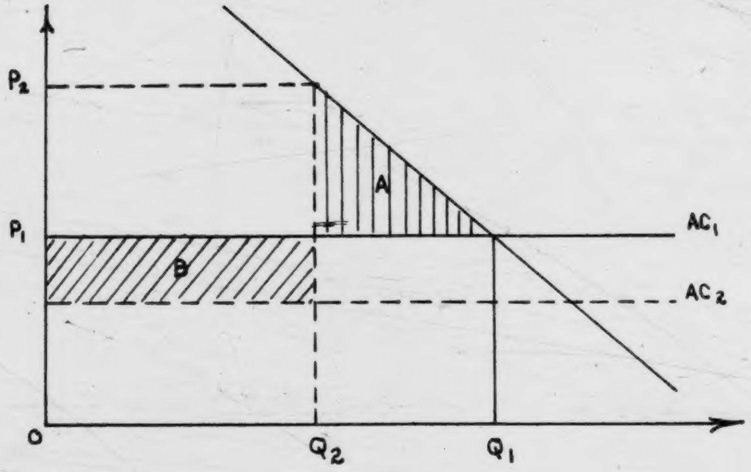
[2] This trend is comparable to the provisions in the Competition Act, s. 64(2).

APPENDIX I

Economies and Market Power



See: Williamson, O.E., "Economies as an Antitrust Defense: The Welfare Tradeoffs", (1968) 58 Am. Econ. Rev. 18.

1. Before the merger, price is at the competitive level, P_1, and equal to pre-merger cost, AC_1.
2. The merger creates market power, price rises to the supracompetitive level P_2, and outputs falls to Q_2.
3. The consumer surplus lost, which is not redistributed to producers, is the triangular shaded area A, called the deadweight social loss.
4. If the merger is accompanied by efficiencies that reduce cost to AC_2, the resource savings is the rectangular shaded area B.
5. The net welfare effect is the different (B - A).
6. The outcome is a function of:
    - (a) The relative increase in P,
    - (b) The relative decrease in AC, and
    - (c) The elasticity of demand.

7. Williamson shows that the effect of a 20% increase in price is offset by a cost reduction of only 1% if elasticity is 0.5; 2% if elasticity is 1.0; and 4% if elasticity is 2.0. (*Ibid*., at p. 22).

See: Williamson, O.E., "Economies as an Antitrust Defense Revisited", (1977) 125 *U. Pa. L. Rev.* 699, at p. 710, for a discussion of the qualifications to his original analysis.

Williamson outlines the criteria to be evaluated if his "maive" model is to be employed for policy considerations:

(a) Would internal growth, rather than merger have naturally led to economies?

(b) Will the merger foster other mergers?

(c) The effect of the merger on non-merging firms,

(d) The marginal utility of a dollar to the producer versus consumer, and

(e) The effect on political power (macro-concentration issue).